

**The Influence of *Shariah* (Islamic Principles) Corporate Governance on Cross-Border  
Merger and Acquisitions Involving Islamic Companies in the Gulf Countries**

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**A Thesis Submitted to De Montfort University in Fulfilment of the Requirements for  
the Degree of Doctor of Philosophy**

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## DECLARATION

I, Wardah Bindabel, hereby declare that I am the author of this thesis entitled *The Impact of Shariah (Islamic principles) Corporate Governance on Cross-Border Merger and Acquisitions involving Islamic Companies in the Gulf Countries*. It contains no material that has been submitted or accepted previously for any academic degree.

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**WardahBindabel**

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**Date**

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## ABSTRACT

The central aim of the research is to examine whether cross-border Merger and Acquisitions (M&A) involving Islamic financial companies in three Gulf countries and non-Islamic financial companies from the Western countries is influenced by *Shariah* Corporate Governance (CG). Cross-border M&A is a corporate level strategy to achieve organisational growth and expansion through accessing new markets and additional strategic resources (knowledge, technology and complementary skills). Islamic financial companies in the Gulf region are keen to engage with non-Islamic financial companies beyond the Islamic world to benefit from the cross-border M&A. However, for Islamic financial companies to operate at global scale and attract resources, investors, regulators, customers, and other stakeholders should trust that strong CG principles are embedded in the organisation's core. CG theory suggests that good corporate governance enables corporations' access to external financial resources if CG mechanisms provides a clear enforceability of stakeholders' rights with complementary robust legal system.

Existing literature suggest that both Islamic and non-Islamic financial companies operate in different institutional, political, cultural, religious, and regulatory environments; which adversely affect the extent to which these two sets of companies could mutually engage in a successful cross-border M&A. In the context of Gulf countries, for example, there is no distinction between the state and religion and there is a stringent requirement to comply with the *Shariah*, however, the existence of conflicting opinions on Islam has resulted in varying views with regards to what qualifies as Islamic finance that has led to a latitude of multiple interpretations of *Shariah* principles by *Shariah* scholars and *Shariah* Supervisory Board. Also, Islamic financial companies are more likely to be considered as social entities than a commercial enterprise, which differs from the Western view. Consistent with the above context-based literature and drawing on the stewardship, agency and stakeholder theories, this study seeks to answer the key research question '*how Shariah corporate governance influences cross-border M&A between Islamic and non- Islamic financial companies?*'

The study employs a qualitative approach to obtain and analyse data from interviews with 40 respondents (Board of Directors members, Lawyers and *Shariah* Scholars) mainly selected from nine banks and six insurance companies in the three Gulf countries - Saudi Arabia, Kuwait and United Arab Emirates. The key findings were: 1) there are variations between the three countries in terms of how the conventional CG model is practised, the extent to which Islamic CG model is adopted, and in the level of employees' awareness of the CG principles; 2) Incorporating Islamic principles in business practices is primarily determined by the interpretation of *Shariah* by *Shariah* scholars and Board but these tend to be non-standardised and at times problematic; 3) In Saudi Arabia and Kuwait, companies tended to have weaker system of disclosure (in particular *Zakat*) and smaller Board dominated by family and less qualified members than the UAE; 4) *Sukuk* is the most widely used but costly, Islamic financial instrument in cross-border M&A activities as it fully complies with *Shariah* principles where as *Tawarruq* is considered questionable in terms of *Shariah*; and 5) there are several barriers, identified in Chapter five, which need to be addressed when considering cross-border M&A between these two sets of the companies.

The study makes several contributions to theory, policy and practices. Its significant theoretical contributions includes: a) as far as existing literature is concerned, this study is the first to examine the influence of the Islamic CG principles on cross-border M&A between Islamic and non-Islamic financial companies; b) Prior research on corporate governance has addressed M&A in developed and emerging countries, however, this is the first study to develop a CG model which seeks to improve our understanding of the complex issues involved in the process of cross-border M&A between Islamic and non-Islamic financial companies; and c) very limited studies have addressed agency, stewardship and stakeholder theories in the context of the development of behavioural *Shariah* CG model in a critical manner. The study has policy implications, for instance, it highlights the need to create stronger standards of Islamic CG and more standardised interpretation of the *Shariah* in these companies to enable them to operate on a global scale. In terms of practical contributions, the study offers implications and recommendations for management and investors alike based on the study findings.

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## Glossary of Arabic Terms Used

Arabic terms	Meaning in English
<i>Adalah</i>	Justice
<i>Allah</i>	God
<i>Al-Warq</i>	Money note
<i>Amanah</i>	Trust or responsibility of fulfilling one's obligations due to Allah
<i>Fatwa</i>	An Islamic religious opinion, ruling or provision given by an authorised person on a matter of Islamic law to who seeks it
<i>Fiqh</i>	Islamic Jurisprudence
<i>Fiqh Al-Muamalat</i>	Understanding of rulings and precepts of economic transactions and activities
<i>Gharar</i>	Uncertainty
<i>Hadith</i>	Sayings of the prophet Muhammad (s.a.a.w)
<i>Halal</i>	Permissible or lawful
<i>Hanafi</i>	It is one of the four religious Sunni Islamic schools
<i>Hanbali</i>	It is one of the four religious Sunni Islamic schools
<i>Haram</i>	Unlawful, prohibited or forbidden
<i>Ibadat</i>	Worship
<i>Ijarah</i>	Instalment leasing.
<i>Ijma</i>	The consensus that is, acceptance of a matter by a specified group of <i>Shariah</i> scholars or jurists
<i>Ijtihad</i>	The process of making a legal decision by independent interpretation of qualified <i>Shariah</i> scholar, with respect to an issue on which there is little or nothing in the <i>Qur'an</i> or the <i>Sunnah</i> .
<i>Iklas</i>	It is singling out Allah with one's intention in all acts of worship
<i>Itqan</i>	To work in order to obtain the higher quality
<i>Jafari</i>	It is a religious Shia school of thought
<i>Khilafah</i>	religious successor
<i>Maliki</i>	It is one of the four religious Sunni Islamic schools
<i>Maqasid al-Shariah</i>	The general purposes and wisdom behind all <i>Shariah</i> rulings.
<i>Maslahah</i>	General benefit, interest or advantage
<i>Mirath</i>	Inheritance
<i>Muamalat</i>	Transactions
<i>Mudarabah</i>	An Islamic finance contract based on partnership in which one partner finances the project and the other provides management and expertise.
<i>Mudarib</i>	The manager with whom the profits are shared based on <i>Mudarabah</i> contract.
<i>Murabahah</i>	Contract of sale in which an asset or good is sold at a specified profit margin.
<i>Musharakah</i>	Partnership contract based on profit/loss sharing in which both parties contribute capital and may form a joint management.
<i>Mutanakisah</i>	Diminishing

<b><i>Qiyas</i></b>	Analogical deduction, which seeks to establish a similarity between new cases and early practices found in the <i>Qur'an</i> or <i>Sunnah</i> .
<b><i>Qur'an</i></b>	The last revealed word of Allah to the Prophet Muhammad (s.a.a.w) by the Angel Gabriel.
<b><i>Qur'anic text</i></b>	<i>Qur'anic</i> verse
<b><i>Rab-Almal</i></b>	The capital provider
<b><i>Riba</i></b>	Interest
<b><i>Shafii</i></b>	It is one of the four religious Sunni Islamic schools
<b><i>Shariah</i></b>	Islamic law
<b><i>Shia</i></b>	A Muslim who follows the Shia branch of Islam
<b><i>Shura</i></b>	The principle of consultation
<b><i>Sukuk</i></b>	Islamic interest-free bonds, they represent ownership of well-defined existing and tangible assets, usufruct and services.
<b><i>Sunnah</i></b>	It is the verbally transmitted record of the teachings, deeds and sayings, silent permissions (or disapprovals) which are the transmitted reports by the Prophet Muhammad (s.a.a.w)
<b><i>Sunni</i></b>	A Muslim who follows the Sunni branch of Islam
<b><i>Shuratic process</i></b>	Decision-making process by interaction, integration with all stakeholders to achieve a creative evolution.
<b><i>Ta'wil</i></b>	Interpretation or allegorical interpretation to extract the hidden meanings
<b><i>Tafseer</i></b>	Exegesis of the Qur'an
<b><i>Takaful</i></b>	A Shariah compliant insurance alternative to conventional insurance in which money is pooled and invested.
<b><i>Tawarruq</i></b>	It is an Islamic instrument that facilitates converting an asset into money. In this contract, the seller arranges a transaction by selling a commodity to the client for deferred payment. The institution then sells the commodity, as an agent on behalf of the client to a third party, in the market and then credits the price to the account of the client.
<b><i>Tawhid</i></b>	Oneness of God
<b><i>Zakat</i></b>	An obligatory payment is paid annually to charitable causes to purify yearly earnings on all surplus wealth

## ABBREVIATIONS

<b>AAOIFI</b>	The Accounting and Auditing Organization for Islamic Financial Institutions
<b>BOD</b>	Board of Directors
<b>CG</b>	Corporate Governance
<b>IFI</b>	Islamic Financial Institutions
<b>IFSB</b>	The Islamic Financial Services Board
<b>KW</b>	Kuwait
<b>M&amp;A</b>	Merger and Acquisition
<b>OECD</b>	The Organisation for Economic Co-operation and Development
<b>SA</b>	Saudi Arabia
<b>SSB</b>	<i>Shariah</i> Supervisory Board
<b>UAE</b>	The United Arab Emirate

## CHAPTER ONE: INTRODUCTION

### 1.1 Introduction

Merger and Acquisition (M&A) occurs when an operating enterprise is involved in the business of some other company in the same industrial sector by completing takeover through acquisition or having partial control on the firm's affairs through the merging process (Blackburn et al., 1990). International M&A across countries have major implications for firms entering new markets in terms of earning profits and increasing the shareholders' dividends while enjoying the benefits of cheap labour (Reuer et al., 2004; Rossi & Volpin, 2004). Since 1990s, there has been rapid growth in cross-border M&A among firms in various countries (Shimizu et al., 2004; Wang & Wong, 2009). Research have shown that with the increasing trend of globalisation, many organisations operating in both the developed and developing countries are expanding their business operations rapidly across international borders to exploit the available business opportunities (Eckbo & Thorburn, 2000). This results in increased economic activities that positively impacts overall economic growth and development (Chatterjee, 2000) and hence signifies an increased importance of cross-border M&A in the present business world.

However, in the context of Gulf Co-operation Council countries, M&A practices occurring between Islamic and non-Islamic financial business requires a distinct approach as paying and receiving interest is prohibited in Islam (Lewis, 2001). Major developments in Islamic business system are currently centred on financial institutions (Moore, 1997; Siddiqi, 2006; Wilson, 2013); and this provides motivation to study cross-border M&A in financial sector, specifically looking at banks and insurance business in the three selected Gulf countries ( more on this in Section 1.6)

The recent KPMG (2015) survey of the executives identified the motivations for cross border M&A, the main sectors of interest and the success factors. This survey found that the need for customer growth (42%) and the need to consolidate core businesses or respond to competition (38%) were main motivating factors. The sub-sectors which were found to be most attractive for M&A were: financial technology (26%), banking (21%) and insurance (17%). The key success factors considered by executives in order of importance were: the well-executed integration plan 39%, correct valuation/deal price 31%, effective due diligence (18%), and positive economic conditions 11% (KPMG, 2015).

Companies look for an existing global representative in the current wave of globalisation to expand their customer base and businesses (Moeller & Schlingemann, 2005). There are many factors that contribute to cross-border M&A, such as (i) the tendency in the emerging country businesses to invest abroad; (ii) creating synergy between or diversifying businesses; (iii) capitalising on growth opportunities; (iv) harnessing complimentary resources; (v) gaining larger market share; (vi) establishing economies of scale; (vii) avoiding undervaluation of target firms; (viii) obtaining intangible assets such as know-how and knowledgeable employees and (ix) gaining freedom not available in their domestic economic environment (Eckbo & Thorburn, 2000; Altunbas & Marques, 2008).

The long-term trend of cross-border M&A deal volumes have consistently been around 2000 deals per year since 2009 and there has been an increasing trend of cross-border M&A in the emerging economies (Equiteb, 2015). This trend favours strengthening of the links between developed and emerging countries (Buch & DeLong, 2004; Muller, 2006). However, Moeller & Schlingemann (2005) and Stahl & Voigt (2008) observed factors that work against cross-border deals such as cultural differences, high information asymmetry and the need for cost sharing between headquarters and international divisions creating agency problems. Barkema & Schijven (2008) and Oak & Dalbor (2009) have concluded that cultural clashes have negative impact on M&A transactions. The cultural differences are very difficult to be quantified in the cost of the integration process to derive appropriate premium for determining the target price and



for the purpose of due diligence. Therefore, it is important to understand whether cultural differences could influence cross-border M&A between Islamic and non-Islamic financial companies.

Different countries, therefore, may have different principles, procedures and business practices, which may be explicit or implicit, depending on their cultural, religious and ethical frameworks (Forstmann, 1998; Georgieva et al., 2012) and these may pose challenges for firms' cross-border expansion strategies (Thomas & Ely, 1996; Keong, 2002). Here the focus is on corporate governance, that is, the way in which a company executes its operations following established standards of fairness, accountability, transparency, disclosure and responsibility.

In this study, it is argued that cultural and religious differences influence corporate governance (CG) practices differently across the globe. Thus it would be important to examine to what extent different corporate governance models influence cross-border M&A as the latter contributes not only to the growth and expansion of the firms but also the countries in general (Vafeas, 2005). Research also shows that increased economic activities in the developing countries could be helpful in improving CG (Gereffi et al., 2005). In any cross-border M&A deals, the target firm generally adopts the accounting standards, disclosure practices, and governance structure of the acquiring firm (Bris et al., 2008). Also, Bris & Cabolis (2008) have shown that a higher merger premium can be achieved when the acquirer's country has stronger shareholder protection and accounting standards. This result is consistent with the findings of Gompers et al. (2001) and Cremers & Nair (2005) that there is high correlation between improvements in transparency and accountability and higher stock returns. Through improving the reputation and transparency, domestic institutions can create competitive advantage across the national borders by increasing their trustworthiness in the eyes of the market intermediaries who supply information globally (Luo & Tung, 2007). It, therefore, helps the firms in the developing world to successfully gain access to the markets of developed countries and increases their revenues and profitability (Moeller & Schlingemann, 2005). Similarly, the target firms benefit from cross-border M&A

through strengthening of their own governance practices to match the governance structure of the acquiring firm (Doidge et al., 2007).

Corporate governance in a particular country is shaped by its culture, history and religion (Haniffa & Cooke, 2002; Licht et al., 2005). This implies that organisational activities in different countries are characterised and influenced by contextual dimension such as religion and social traditions, which in turn affect their behaviour, values and ethical perspectives (McGuire et al., 2011). For example, in Islamic countries, it is widely assumed that there is no distinction between religious and secular affairs (Islam & Hassain, 2003; Brammer et al., 2007) these can manifest in commonality between individual and corporate morality and ethical practices. Thus, Gulf countries, which are Islamic, adopt a CG framework that reflects the Islamic values embedded within local/national culture (Baydoun et al., 2012). Furthermore, the existing literature points out that M&A between firms in Gulf countries and Western countries offer considerable challenges for CG, such as: family-owned and managed businesses; Government intervention in private sector; political system based on monarchy; legal system based on Islamic law and social practices followed by Islamic society (Al-Nodel & Hussainey, 2010; Aljifri & Moustafa, 2007). For instance, in the Western countries, a company is seen as a separate legal entity different from its owners and managers (Pickering, 1968), and this can pose challenges when there is any engagement between Islamic and non-Islamic financial companies. In this study, for sake of simplicity, we may use religion as a convenient proxy for culture though this is likely to miss the rich cultural diversity within commonly employed religious classification such as 'Protestant' or 'Islamic' (Licht et al, 2005). Assumption of uniform CG, even across Gulf countries can be problematic and the CG, even in these Islamic countries may have varying practices based on varying interpretation of *Shariah* (Hameed et al., 2006). Also, the issue of CG needing to be based on principles rather than rules and regulations has been debated among business communities and leaders (OECD, 1999). A parallel situation can also exist in *Shariah* CG, where some scholars consider Islamic law literally in proclaiming their decisions instead of basing them on the principles. These factors can lead to diverse CG practices and transactional practices

even in Islamic countries. So, it is important to examine the influence of culture and religion influence the CG in the context of the cross-border M&A.

The companies in the Gulf region are deeply interested in seeking cross-border M&A with companies around the globe, primarily motivated by their developmental needs in terms of: finding investment avenues; access to advanced technology; technical, marketing and managerial expertise in different sectors of the economy (Dubey & Kummer, 2016). Current focus of the Western world on CG could increase transparency and accountability, enhances investor protection, and could decrease agency costs (Vafeas, 2005). With the increasing adoption of *Shariah* CG in the Islamic world and many Western companies showing interest in Islamic products, it would be useful to understand the differences between conventional and *Shariah* CG, and how this can affect cross-border M&A.

## **1.2 The Motivation of the Study**

This study is the first of its kind to explore the influence of *Shariah*-based CG on cross-border M&A between Islamic financial companies in the Gulf region and non-Islamic financial companies from the Western countries. CG is one of the widely-researched concept due to its relevance for well-functioning and sustainability of businesses globally (Aras & Crowther, 2008). The issue of how the Islamic CG can be integrated or complement with the conventional CG in the context of cross-border M&A is rarely studied. Therefore, this research seeks to fill this gap by examining how the Islamic approaches to good CG based on the *Qur'an* and *Sunnah* and how different interpretation of *Shariah* principles by *Shariah* scholars influence the cross border M&A of Islamic and non-Islamic financial companies.

Adoption of good CG and practices are crucial for the success of cross-border M&A (Martynova & Renneboog, 2008), with an added layer of compliance when dealing with Islamic financial companies to stand the test of compliance with the *Shariah* principles. Currently, there is an active debate on creating a better understanding of how to carry

out business transactions in the light of *Shariah* (Abuznaid, 2009; Usmani, 2007). *Qur'an* and *Sunnah* provide guidance for good CG and efforts have been intensified in the Islamic society to contribute and provide deeper and wider understanding of social, economic and political disciplines of Islam.

Being a complete code of life for Muslims, Islam offers solutions for both business and society. In terms of business, for example, *Shariah* prohibits all transactions involving *Riba* (interest) during the conduct of any business and allows sharing of profit and loss including any risk associated with the business deals (Chapra, 1998). Sharia principles such as these form the basis when conducting M&As locally and internationally and these are very different from the conventional CG. Thus, understanding to what extent such principles are deployed in financial institutions of the three Gulf countries is of interest to this research.

Indeed, most religions have the same fundamental principles governing good CG practices such as fairness, accountability, transparency, truthfulness and sincerity (Volonte, 2015). However, the implementation of Islamic principles varies from country to country due to different interpretations by different *Shariah* scholars. The *Shariah* CG is principally based on two sources: (i) *Fiqh* (knowledge of the Islamic rulings), which would be based on the different Islamic schools of thought such as the *Sunni* schools of *Hanafi*, *Maliki*, *Shafii* and *Hanbali* or *Shia* schools such as *Jafari* etc. (Reinhart, 1983); and (ii) *Fatwa* (a scholar's opinion from an Islamic point of view). The points of possible divergences can therefore arise from the following of the different schools of thoughts as well as the experience, wisdom and the conservative or liberal outlook of individual scholars in considering issues in accord with *Shariah* principles. In fact, such differences in interpretations of the sharia law and principles can pose challenges in the process of cross-border M&A between companies of different cultural and religious backgrounds including those within Islamic countries.

### 1.3 Aims and Objectives of the Study

The study aim to investigate the extent and how *Shariah* corporate governance influences cross-border M&A between the Islamic financial companies in three Gulf countries (Saudi Arabia, Kuwait and UAE) and non-Islamic financial companies in the Western countries. The study pursues the following research objectives to achieve the aim of the research.

- i. To identify how the Islamic corporate governance is constituted and how it is different from the conventional corporate governance model? This research objective would help to understand to what extent the CG models are compatible.
- ii. To examine the extent Islamic CG is adopted by the Islamic financial companies.
- iii. To investigate how the current Islamic CG mechanisms practices in the three countries facilitate or constrain the process of cross-border M&A and which cultural factors influence the Islamic CG mechanism?
- iv. To examine the extent *Shariah* principles are applied in business practices of Islamic financial companies and to identify the active player in interpretation and enforcement of these principles?
- v. To identify the main barriers for effective implementation of the *Shariah*- based Islamic corporate governance principles in business and in the context of cross-border M&A.
- vi. To examine the nature and influence of the Islamic legal corporate structure on the decision- making process in Islamic financial companies
- vii. To identify the M&A financing instruments used in the context of cross-border M&A.

## **1.4 Research Questions**

In line with the research aim and objectives, the following research questions were formulated. The research questions were designed in such a way as to explore, and further to understand the nature of the *Shariah*-based CG in influencing cross-border M&A. Hence, essential dimensions of the Islamic CG within its context are to be examined through the following research questions:

1. What constitutes Islamic CG and how does it differ from the conventional CG model? In other words, is there compatibility between the conventional and Islamic CG models?
2. To what extent the Islamic CG is adopted by the Islamic financial companies?
3. Do the Islamic CG mechanisms facilitate or constraint in the process of cross-border M&A? what cultural factors influence the Islamic CG mechanisms?
4. To what extent are *Shariah* principles applied in business practices of Islamic companies? Who are active players in interpretation and enforcement of these principles?
5. What are the main obstacles for effective implementation of the *Shariah*- based Islamic CG principles in business and in the context of cross-border M&A?
6. What form does the Islamic legal corporate structure takes and how does it shape the decision making in Islamic financial companies
7. Which Islamic financial instruments are likely to be used in the context of cross-border and why?

## **1.5 Justification of the Chosen Industries and the Research Area**

This research is limited to the largest three Islamic Banks and two Insurance companies in each of the three Gulf counties, which are quoted in their respective stock markets. The financial sector involving the banking and insurance organisations were selected

for this study for two reasons. First, the sector provides critical cases which show, comparatively, strong manifestation of the *Shariah* CG. Second, the issues of cross-border M&A between the Islamic and non-Islamic financial companies might be complicated and problematic because of the ways in which firms conduct business, such as engaging in interest payable and interest receivable products, and managing of risky transactions involving financial derivatives could be not only different but also prohibited in the study context. Third, the financial sector is the second major contributor to the GDP after oil and gas sector, typified by concentrated ownership, largely domestically owned and protected but also has been growing (Al-Obaidan, 2008; Yu & Hassan, 2008). Fourth, Islamic financial sector has attracted investors worldwide, which has led to increase in its business and economic activities both regionally and globally (Islamic Financial Services Board, 2015). Thus, the sector and the chosen cases provide rich context to examine the cross-border M&A between Islamic and non-Islamic financial companies because of their wider significance.

Given the context of three Gulf countries, this research was motivated to examine whether there are variations in which the Islamic CG model and principles being applied and the reasons which may explain such variations. Further motivation for the study was to explore to what extent existing conventional theories such stakeholder, stewardship and agency, which may explain the CG practices and stakeholders' behaviour, are useful to understand the Islamic CG.

## **1.6 The Structure of Thesis**

The thesis is organised into six chapters.

Chapter one outlines the research background, research purpose, research objectives and questions and justification of the choice of the financial sector and cases from both the banking and insurance industries in the three Gulf countries.

Chapter two presents the review of a wide range of literatures in substantive and critical manner. The literature review covered issues relating the conceptualisation of the corporate governance, its mechanisms, corporate legal structure in the study context, Islamic CG, development of Islamic finance and three related theories.

Chapter three presents the research methodology used in this study including the research paradigms, research approaches, research strategy, sample selection, data collection methods, data analysis and ethical issues. The empirical data were collected through interviews with 40 respondents with different roles (managers, legal advisors and sharia scholars) from 9 banks and 6 insurance companies quoted in the stock markets of Saudi Arabia, Kuwait and United Arab Emirates.

Chapter four discusses the findings and the analysis of the empirical data. The analysis follows qualitative, interpretative, approach using themes generated from the data gathered and from both theoretical and empirical literatures.

Chapter five provides the summary of the key findings, conclusions, theoretical contributions, implications and recommendations for various stakeholders, limitations and ideas for further study as well as a final note on how the research objectives and questions were met.



## **CHAPTER TWO: LITERATURE REVIEW AND THEORETICAL FRAMEWORK**

### **2.1 Introduction**

This chapter undertakes the review of a body of prior studies carried out within three main areas, which are Conventional CG, Islamic CG and Cross-Border M&A. There is a great deal of attention given to CG particularly since late 1980, after the collapse of companies in different countries such as Rothwells Ltd, Enron, WorldCom, Global Crossing and Adelphia etc. (Bosch, 2002; Parker, 2005; Tricker, 2015) posed a big challenge to business enterprises, especially those in developing countries, to adopt better CG practices (Chen & Findlay, 2003). In addition, the financial crisis that occurred in 2008 affected many countries, including the Gulf countries (Claessens et al., 2000) and emphasised the need for good CG.

Adoption of CG becomes an important factor for developing countries firms as it enables them access to the developed world via cross-border M&A and this is directly linked with the economic growth and development (Briset et al., 2008; Weitzel & Berns, 2006). Bris et al. (2008) found that there is a high correlation between good practices of CG adopted by a firm and cross-border M&A. Similarly, Martynova & Renneboog (2008) found a strong correlation between transparency and cross-border M&A success. The argument here is that good governance is likely to increase not only the value of the firms but also the industry due to increased and successful M&A activities. Successful M&A activities enable developing countries firms to successfully penetrate the markets of developed countries and increase their revenues and profitability (Moeller & Schlingemann, 2005). Besides good CG, a greater understanding of the following critical success factors is essential for a company to succeed in a cross-border M&A.

CG is shaped by a particular country culture, history and religion (Haniffa & Cooke, 2002; Haniffa & Cooke, 2005; Licht et al., 2005), this implies that people who operate

organisations in different countries are characterised by different dimensions such as education, religion and traditions, which affect their ethical perspectives, which in turn affect their decisions (Ely & Thomas, 2001; Licht et al, 2005; Haniffa & Cooke, 2005; McGuire et al., 2011). Because of the different cultural background, corporations in Gulf countries offer challenges in adoption of the conventional CG and in any cross-border M&A. This is because firms in GCC countries are typified by different features such as predominance of family-owned businesses, Government intervention in private sector, political system based on monarchies, legal system based on *Shariah* (Davis et al., 2000; Rice, 2003; Al-Nodel & Hussainey, 2010; Baydoun et al., 2012). Understanding the principles and practices which are based on the religion and culture may provide better understanding how to harmonise principles of CG to facilitate cross-border M&A.

This chapter discusses the definition, models and mechanisms of the conventional CG, followed by the CG practice in Gulf countries and the underlying *Shariah* CG principles, followed by sources and principles of *Shariah*, CG model informed by *Shariah* and how Islamic companies are directed, controlled and operated, Islamic financial instruments and the overall theoretical framework consisting of Stakeholder, Stewardship and Agency theories.

## 2.2 What is Corporate Governance?

The practice of CG is as old as trade and the issues that this concept addresses have been discussed long time ago, however, it is relatively new in the academic field (Cadbury, 1992; OECD, 1999; Tricker, 2015). Scholars' definitions of CG vary, based on (i) which CG model has been adopted in different countries; and (ii) the laws of the country of jurisdiction. For example, the Anglo-Saxon model of CG is prevalent in the countries which emphasise shareholder values. In contrast, Japanese model emphasise a wider stakeholder group.

A broader definition of CG can be characterized as a system of three dimensions: principles, processes and outcomes (Gunay, 2008). Furthermore, another broader definition of CG was presented by Sir Adrian Cadbury (1992), head of the Committee on the Financial Aspects of CG in the United Kingdom: as “the system by which companies are directed and controlled”. Steiner & Steiner (2012) expanded on this definition, referring to CG as an effective control system within organizations, where managers effectively implement business strategies and plans to maximise shareholders’ wealth. CG is, thus mainly concerned with accountability, transparency, fairness, disclosure and responsibility, regardless of the type or nature of the business.

In respect of CG in relation to management, situations may arise where the ownership of the firm is different from the management (Claessens & Yurtoglu, 2012); therefore, developing required processes and procedures through which the firm is controlled and governed would be important (OECD, 1999). Economic scientists such as Monks & Minow (2004) have defined CG as the relationship between various participants (CEO, management, shareholders and employees). Another perspective by Blair (1995), presented CG as a set of legal, cultural and institutional arrangements while Freeman & Evan (1990) have defined CG as consisting of a framework of voluntary multi-lateral agreements within an organisation. These definitions, basically, focus on aligning the principal-agent objectives in a system with checks and balances to achieve the required transparency and accountability.

A narrower concept of CG, given by Shleifer & Vishny (1997, p.737) states, “corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment”. This definition could be expanded to include solutions to the problems and settlement of the conflicts and clashes between various shareholders, for example, La Porta et al. (2000) defined CG as a group of mechanisms through which outside investors secure themselves from inside investors.

According to Claessens & Yurtoglu (2012) there are two approaches to CG. The first focuses on behavioural patterns of humans in the firm, such as Boards of Directors,

composition of Board of Director, the roles of multiple shareholders, stakeholders and external auditors in relation to the firm performance and growth (Kaen, 2003; Praveen, 2004; Monks & Minow, 2004; Cornelius, 2005; Claessens, 2006). The second focuses on normative framework which considers capital markets rules that lead to investors' protection and creditors' rights, such as disclosure and accounting, reporting and protections of minority shareholder rights (La Porta et al., 2000; Claessens, 2006; Hambrick et al., 2008; Bondy et al., 2008). Some authors such as Oman (2001) and Council (2010) have defined CG to explicitly include Corporate Social Responsibility (CSR) and sustainability concepts.

Based on the above debate, firstly, Davies (2012) affirmed that CG provides guiding principles to manage the business organisations regardless of their type, whether commercial or otherwise. A well-understood principles and policies help to guide managers' and employees' behaviour in certain circumstances. Charantimath (2005, p.219) also asserted that "CG brings the right people together at the right time to discuss the right (important) things".

Secondly, Brooks (2004, p.33) defined CG as "the structure, which specifies the distribution of responsibilities and rights among different corporate participants in corporation, such as, the Board, the managers, shareholders and other stakeholders and spells out the rules and procedures for making decisions on corporate affairs". Therefore, it also offers the structure through which the organisational objectives are set and the ways of meeting those objectives are planned.

Kaen (2003) defined that CG is about who manages firms and why. This definition is concerned with supervising and managing the organisations' activities. These thoughts are mainly concerned with behaviour of corporations focusing on several measures such as performance, efficiency, growth and the rights of shareholders and other stakeholders (Classes et al., 2000). However, these vary from one country to another based on their orientation and the ways in which the legal systems work (Shleifer & Vishny, 1997). On

the other hand, a minimalist approach to CG focuses on the set of rules directing the corporation, which are derived from the legal and judicial systems, financial and labour markets. This is supported by Baker & Anderson (2010) as they stated that CG is the processes and systems applied to control and direct a firm to develop performance and accomplish sustainable value of its shareholder.

In contrast, some Islamic scholars attempted to provide explanation of CG from an Islamic perspective, such as Elasrag (2014) who noted that CG concept from Islamic perspective does not vary much with conventional CG, except prohibition of certain products and practices as well as concern for all stakeholders rather than just the shareholders and therefore be seen as a special case of a wider theory of decision-making that utilizes the Islamic socio scientific epistemology, which is premised on divine God oneness (Choudhury & Hoque, 2006). Moreover, Sourial (2004) noted that Islamic law contain numerous guidelines on how to deal with economic transactions that includes moral conduct of Muslim.

Considering the range of definitions on CG, a number of researchers including Aguilera and Jackson (2010); Claessens & Yurtoglu (2013) and Matoussi & Jardak (2012) debated the question whether a common, international framework of CG would be optimal for all countries.

### **2.3 Corporate Governance Models**

CG models are adopted in different countries to achieve value-oriented management and control of companies. Comparative research has found that one size of CG would not equally fit all countries (Corbetta & Salvato, 2004; Davies & Schlitzer, 2008). As Shleifer & Vishny (1997) have noted, there are two distinctive patterns of CG in developed countries: (i) an approach which focuses on shareholders and relies on the free market as corrective mechanism or the “outsider system”, such that the management team intend to operate for the purpose of maximising the shareholders’

return on investment such practice is adopted in US and UK; and (ii) an approach which focuses on all stakeholders or the “insider system”, such that the management takes a wider perspective and looks after the interests of one or more groups of stakeholders, such as, the employees, suppliers, lenders, public authorities and public at large. The first, also known as the Anglo-Saxon model is found in the Anglo-Saxon countries like UK, US, Canada, and Australia. The second, which can be referred to as the Combination model, as it combines the Anglo-Saxon model with national culture, values, regulations, is found in continental European countries like Germany, Holland, France, etc., and Japan.

### **2.3.1 Anglo-Saxon Model**

Anglo-Saxon approach of CG focuses on protecting the interests of organisations’ shareholders (Cernat, 2004). Mueller (2006) considers shareholders or the capital providers as the owners of the company (principals), who appoint the managers (agents) to run the business on their behalf and generate wealth for the owners. Therefore, the interest of the owners is paramount.

The Anglo-Saxon model was built on a strong foundation of capitalism principles. Due to this reason, it has been adopted by countries that have adopted original forms of capitalism (Lutz & Eberle, 2007). Anglo-Saxon approach relies on free market as the correction mechanism as it is characterized by less regulated financial and labour markets (Chabal, 2013). When an organisation has weak CG, it has a high level of agency costs which increases over a period of time due to failure to account for these costs (Moerland, 1995). This affects the growth of the company and its shareholders’ return of investment, making the company an attractive target for takeover by another player in the industry, which can turn the company around by strengthening the CG. The market forces, therefore, provide a strong incentive for working towards strong CG and minimising agency costs to ensure survival and growth of the organisation (Drobetz et al., 2004). But such models fail to account in the context of market imperfections and heavy state involvement in the business environment. Further, Kulik (2005) and Driver & Thompson (2002) have argued that to view an organisation’s sole purpose of

existence as only adding value to the shareholders is a very narrow conception and severely limits the role of large organisations in the social framework.

Cost of capital is expected to be adjusted through the market mechanism (Healy & Palepu, 2001). High cost of capital is associated with weak system of CG and high agency risks. This may lead to less investments' opportunity; reduce profitability and high bankruptcy costs of the organisation (Leland, 1998; Williamson, 2002). Market mechanisms play an important role in translating high agency costs into weak financial performance and this can be considered as a disadvantage of the Anglo-Saxon model.

### **2.3.2 The Combination Model**

The combined approaches consist of different models that emanate from the Anglo-Saxon approach; however, these approaches vary based on the countries culture, values, regulations and religion (Aguilera et al., 2008). For example, the Japanese model of CG pays attention to wider groups of stakeholders; therefore, it is the closest model to the stakeholder theory (Allen & Zhao, 2007). It is seen that the Japanese system of CG is based on social norms, traditions and family values as families originally ran the businesses where shareholders typically have a long-term investment focus (Morck et al., 2000). As the average shareholder tends to hold on to stock for a longer period (8year), managers' decisions are supposed to be focused on adding value to these shareholders.

The French CG model focuses on the welfare of the employees as much as the shareholders of the companies. The French model has a strong foundation on Marxist principles which support the strong labour laws in France (Morin, 2000). It is noted that the labour-oriented CG has traditionally been strong in French corporations and the union members might be represented on the Boards of the companies (Ahlering & Deakin, 2007). However, Goyer (2003) noted that in recent years, CG model in France has seen major movements towards the Anglo-Saxon model. This shift is attributed to

the fact that the American and British financial institutions are gaining growing dominance in the capital market in France. The author stated that that a large percentage of the equity of most of the top companies in France is owned by the owners of these financial institutions. Due to their influence also, the companies are moving towards the Anglo-Saxon CG model.

Similarly, German CG model has seen major movements towards the Anglo-Saxon approach as the most corporations in Germany focus on shareholders rather than other groups of stakeholders (Lane, 2003). Initially, the German model was based on 'codetermination' that involves the labour force, the management and business policies. In addition, emphasis was placed upon the labour or employees as the most prominent group of stakeholders, which required the management to make their decisions based on the impact to the employees (Driver & Thompson, 2002). This model consists of two tier system for management, which are the Board and the representatives of work council to supplement the Board.

Based on the above CG models, it can be said that despite the observed similarities between the developed countries, CG structure and ownership are different. For instance, the long-term ownership orientation by shareholders in Japan and mandatory influence of labour representatives in Germany show some of these differences in the structure and ownership patterns in CG. Most of the CG debate has mainly focused on developed economies. But not much studies exist which focused on the CG in developing and emerging economies albeit with some focused in countries such as China, Brazil, and India. Similar trend in research interest is emerging with the context of developing countries such as Arab countries, Malaysia, Indonesia, Bangladesh and Pakistan who adopt Islamic CG. It may be relevant to ascertain the CG practices in such diverse and emerging places to help in harmonising CG models. Specifically, China has drawn more attention on its CG based on its continued economic growth (Wortman, 1994; Melin & Nordqvist, 2000; Berghe & Carchon, 2003). The following sections focus on China and Gulf countries as examples of emerging models of CG.



### **2.3.3 The Chinese Model**

In comparison to the other models, the Chinese model of CG is quite different from the West (Allen et al., 2005). Chinese CG model has gone through different stages of evolution (Abbott & Snidal, 2000). Initially, post 1949, the Chinese economy was dominated by the state-owned enterprises and the Government was responsible for controlling each and every aspect of the economy (Armstrong & Armstrong, 2001). In the second stage (mid-1980s), the Chinese Government had started implementing privatisation policy. At this stage, the state's role in the business activities had drastically being minimised. During the third stage (1993), the modern corporate structure was implemented and laws and regulations were made to ensure smooth operations in enhancing the employee involvement and distributing authority to them based on their skills and capabilities. Also at this stage, the state shareholders still enjoyed preference over the individual investors within the country. During the final stage (2005), the individual investors were given particular importance and Government of China provided all the necessary facilities to support the investors in order to encourage and promote domestic and foreign direct investment within the country (Yong et al., 2008).

The corporate regulations and laws have helped the Chinese Government to ensure continuous growth of CG within the country. Currently, the CG model in China is focused on balancing the power between individual shareholders within the organisations and state shareholders (Wang et al., 2004). In the present scenario, the shareholders, Board of Directors and management personnel in the Chinese companies are involved directly in implementation of the CG of their respective organisations (Glen & Singh, 2005). The present CG model in China has also helped an increased level of participation of shareholders in the company's business operations. The effective implementation of corporate regulations, legal systems and auditing systems has also increased the trust and confidence of the investors, which has improved the domestic investment within the country and positively impacts the financial performance of the organisations (McDonnell, 2002). As Jomo & Folk (2003) observed, the CG in China has been rapidly improving enhancing the trends of globalisation.

Liu (2006) provided a preliminary survey to better understand the contrasting features of the CG practices in China. The author argued that the China CG could be described as a control-based model where the decision making is in line with the shareholders' interest. He further stated that the dominant CG model adopted by Chinese companies contrasts with the market-oriented model. He argued that this kind of model is damaging the investors' confidence and negatively affecting the development of China stock market. As the study context is typified, to some extent, by control-based model, it would be interesting to explore how such CG influences the cross-border M&A.

Although China has achieved fast economic growth and this has been reflected in the rise of their gross domestic product as well as increased foreign reserves, it is still considered as an Emerging Market Economy (EME) as a result of weak institutional structures as well as underdeveloped and poorly regulated financial sectors (Carrasco & Wililams, 2012). While EMEs such as China, Brazil and India cannot be considered developed countries, their continued progress indicates that the CG models adopted by the specific countries offer some benefits for local organisations.

### **2.3.4 CG System in the Gulf Countries**

Apparently, following the aftermath of 1997 financial crisis of East Asian corporations (Claessens et al., 2000) and the downturn of subprime in 2008-2009 in USA (Verick & Islam, 2010), there has been a call for regional economic development and growth of sound CG among the Gulf countries (Baydounet al., 2012). Local regulatory agencies have started considering a new framework to improve CG in Gulf countries (AlMalkawi et al., 2014). Bauer et al. (2004) highlighted that organisations with better Board and CG translate into better-governed companies. Saidi (2004) further contended that corporations in the Middle East and North Africa (MENA) region must adopt the basic tenets of effective CG. Other factors such as becoming a financial and commercial centre, being the World Trade Organisation (WTO) and the need to have access to

international capital to fund additional growth and globalization of existing business require the GCC countries to improve their CG systems (Alyafi, 2005).

The businesses in Gulf region were safeguarded from financial crisis that affected most of the Western countries and they are yet to adopt best practices of CG as most Gulf institutions are undeveloped due to market imperfections and family ownership (Saidi, 2004; Aulakh & Kotabe, 2008). According to a report by Gulf Business (2015), families own approximately 60-70 % of companies in the Gulf region; hence, there could be reluctance to disclose financial information to the public (Sophia, 2015). Further to this, a study done by BDI in 2013 on Board effectiveness in the Gulf revealed that the level of disclosure and transparency of Gulf corporations was low in areas such as composition and number of BOD in comparison with Western and Asian standards.

It is commonly acknowledged that financial issues are not the only sign of weak CG, but rather environmental, social and human damages are also indicators of the soundness and sustainability of CG (Boatright, 1996; Donaldson & Preston, 1995; Mitton, 2002). Researchers such as Bakhtari (1995), Saidi (2004), Haniffa & Cooke (2005) and Licht et al. (2001) have found that culture and religion have a negative impact on CG practices in MENA region including Gulf countries, which are all Islamic countries. Hidayah (2014) provided empirical evidence, which shows that CG practices rely heavily on cultural and Islamic beliefs. *Shariah* law has been widely used as a guiding principle in CG practices in Gulf countries which is subject to *Shariah* scholars' different interpretations of Islamic principles which might present difficulties in practice (Beckett, 2003; Islam & Hussain, 2003; Chapra & Ahmad, 2002; Hasan 2012). Although Lim et al. (2007) have indicated that there is evidence of Anglo-Saxon and combination models of CG principles applied in this region; there has been strong adoption of *Shariah* CG, which guides the Islamic companies. Therefore, the concept of what is widely known as "Islamic Corporate Governance" is emerging (Chapra & Ahmad, 2002; Choudhury & Hoque, 2006; Lewis, 2005; Choudhury & Alam, 2013) but more empirical studies yet to be conducted how Islamic CG manifest and how different

stakeholders respond to such emergence in practice. Perry (2011) stated that Islamic CG model involves two Boards management, one that is required by conventional law and the other required by *Shariah* law, which is similar to the German CG. Also Japanese, Chinese, Brazilian and Indian companies have embedded their culture and religion in their CG in contrast to the Western countries. But little is known to what extent various stakeholders such as directors, legal advisors and *Shariah* scholar perceive the influence of culture and *Shariah* principle on the adoption of Islamic based CG and in what ways and to what degree the Islamic CG mechanisms are applied in Islamic financial institutions. This research, in part, addresses this gap.

Many researchers including Jones & Pollitt (2004) and Clift (2007) have observed that companies have been trying to develop a CG model that enables them to become an active player in the global market. It is noted that most of the countries with combination models have shown a tendency to move slowly towards the shareholder-friendly policies and frameworks to enable better global integration in the world dominated by the Western companies. In fact, most of the countries have adopted the Anglo-Saxon model to more and less extent necessitating the Islamic companies to better understand the conventional CG so that they would be able to adopt a more formal, standard and consistent *Shariah* CG (Safieddine, 2009) in order to remove uncertainties and be able to integrate into the global market. Bertillo et al. (2013) noted that Islamic financial sectors are trying to formulate a new model of Islamic CG, yet they have been faced with various challenges. This observation begs a question ‘to what extent are Islamic financial institutions in the Gulf countries able to incorporate *Shariah* principles in their CG system. This is one of the research questions this research seeks to answer.

The key features of the different CG models are summarised in Table (2.1), for ready reference.

**Table 2.1: Summary of the Key Features of the Different CG Models**

<b>Model</b>	<b>Anglo-Saxon</b>	<b>Japanese</b>	<b>French</b>	<b>German</b>	<b>Chinese</b>	<b>Islamic</b>
<b>Foundation</b>	Capitalist principles of Anglo-Saxon countries	Traditional and family values	Employee welfares	Employee welfare and Management Co-determinant	Dominated by state owned enterprises	Islam
<b>Purpose of corporation</b>	Protecting the interests of the shareholders	Various groups of stakeholders	Employee welfare as much as the shareholders	Both the labour force and the management	Balancing the power of individual and state shareholders	To safeguard the rights and interests of various stakeholders
<b>Source of CG</b>	Free market as the correction mechanism to minimise agency cost	Based on traditional and families' values	Labour oriented CG system	Constitutional law derived from co-determinant	Based on communal system	<i>Shariah (Quaran &amp; Sunnah)</i> and the concept of prohibited practices
<b>Management</b>	Managers have a very strong sense of duty to act in interest of shareholders	Be loyal and add value to shareholders	Managers do not have a representative responsibility to shareholders	Decisions based on the impact on management and employees	Management and BOD have more authority to protect the interest of shareholders	Management and auditors undertake duties to meet organisational and God's objectives
<b>Board structure</b>	Unitary	Two- tier	Unitary	Two- tier	Two- tier	Two-tier

## 2.4 Corporate Governance Mechanisms

Many scholars have reviewed CG mechanisms, such as Shleifer & Vishny (1997), John & Senbet (1998), Fan et al. (2002), Becht et al. (2003), Huse (2005) and Nikoskelainen & Wright (2007). They have looked at the internal mechanisms within the firm (such as Board effectiveness, owners, shareholders and employees) and external mechanisms

outside the firm (such as legal and regulatory obligations, auditing standards and quality of disclosure).

Previous researchers such as Haniffa & Hudaib (2006); Bozec & Dia (2007) and Koh et al. (2007) have identified the important CG mechanisms as ownership structure, dual chair, and composition of Board and director independence, integrity in financial reporting, annual disclosure and external auditors. These mechanisms are discussed below.

#### **2.4.1 Ownership Structure**

There are debates on the issue of separating ownership from control in modern corporations, since ownership structures dominate CG models (Claessens et al., 2000; Lemmon & Lins, 2003). Ownership structure is one of the main aspects of CG that plays an important role in cross-border M&A (Aguilera & Dencker, 2004; Eugster, 2015). For example, Jensen & Meckling (1976) argued that ownership structures determine the overall control of the organisations, which can influence their performance. Also, in large organisations, there may be conflict of interest between the owners and executive managers in terms of separation of control (Haw et al., 2004).

There are various types of ownership structure such as the large shareholders' ownership, which is common in the public organisations in Western countries and the family or minority ownership structure, which is common in developing countries such as Gulf countries (Othman & Zeghal, 2010).

Certain families control large sets of businesses in the Gulf countries due to strong political, cultural, religion and historical ties with African and South Asian markets (Chahine, 2007; Saidi, 2004). Baydoun et al. (2012) carried out a study on governance practices and found that there is rarely any separation between ownership and

management, as friends and relatives dominate the BOD. Furthermore, Yasin & Shehab (2004) concluded that good CG is determined by high concentrated ownership structure.

However, Eugster (2015) emphasised that with the presence of family control shareholder decreases the likelihood of cross-border M&A. So, it would be interesting to examine how such ownership structure which typifies Gulf firms influence the general CG mechanisms in this region.

#### **2.4.2 Dual Chair**

Dual chair is one of the CG aspects, which usually acknowledges that a person could effectively manage a company by occupying two positions (Chief Executive Officer (CEO) and the BOD Chair) at the same time (Forker, 1992). Many firms in Gulf is family owned and duality is a common feature in these firms (Chahine, 2007; Safieddine, 2009; Al-Hassan et al., 2010). CEO is responsible in managing the organisation, presenting the financial reports, and alerts the Chair of any sensitive issues (Warther, 1998; Carver & Carver, 2009). For example, Organisation for Economic Cooperation and Development (OECD) recommends that CEO and Board Chair roles should be separated and that the chair must be selected from the non-executive directors. Moreover, the roles and responsibilities of CEO and the Chair should be clearly defined (OECD, 1999). Providing distinction and clear job functions may help to facilitate cross-border M&A.

However, some scholars provide a counter argument based on stewardship theory provided by Donaldson & Davis (1990), which suggests that the separation of the two roles might not be essential, because if the roles are combined with clear and unambiguous authority and less interference then effective management can be achieved. In contrast, the agency theory suggests that the CEO and the Chair responsibilities should be separated as this will benefit the company by improving the Board's independence from the management, which will lead to better monitoring (Eisenhardt, 1989). The findings reported above thus are inconclusive regarding dual roles. This thesis, therefore, seeks to examine how assuming two roles (CEO and chair

of BOD) simultaneously compromise the effectiveness of the CG and its influence on organisational performance in the context of Gulf countries.

### **2.4.3 Composition of Board and Director Independence**

The BOD members are key players in providing strategic direction for firms (Abidin et al., 2009; Ho & Williams, 2003). A wider range of expertise, skills and knowledge possessed by a large size BOD improve the quality of strategic decisions (Abeysekera, 2010; Dalton et al., 1998). They can also influence the formation of cross-border M&A by structuring relevant strategies and policies to expand their business abroad (Brewer et al., 2000). Directors' independence has been the factor of immense importance in previous studies in terms of its impact on firm performance and dual chair (Brickley et al., 1994). Moreover, independent directors can achieve superior managerial decisions and long-term performance as they provide more resources, information, and legitimacy to firms (Hillman, et al., 2000; Ibrahim et al., 2003). Yermack (1996) found evidences that firm's value is increased if directors' independence is ensured in the firms. Similarly, Rechner & Dalton (1991) showed that Board composed of independent directors' increase the firm's value. This suggests that independence of the director is one of the important tools of CG.

Literature also provides positive evidences on the relationship between Board independence and M&A. For instance, Byrd & Hickman (1992) found that firms with Boards composed of independent directors have better local deals and helps in cross-border M&A. Similarly, Shivdasani (1993) also found a positive impact of Board independence on these deals. However, in the Gulf countries getting experienced and qualified independent non-executive directors is usually difficult especially in smaller countries (Baydoun et al., 2012). Hence, understanding Board composition, director independence and how to source qualified and experienced independent directors in respect to cross-border M&A is relevant. This will help in creating better formation of new strategies and harmonisation of processes, procedure and policies that will enhance M&A.



#### **2.4.4 Safeguarding Integrity in Financial Reporting**

OECD recommends that all listed companies need to set up audit committee with a minimum of three members including the Chair and must consist of non-executive directors of the company (Collier & Zaman, 2005). Klein (1998) argued that the larger the audit committee size with various experiences, skills and knowledge combination, the better its impact on performance. Also, a valuable committee comprises of independent, committed and qualified members (Beasley & Salterio, 2001). The committee is responsible for reviewing and analysing financial reporting (Abbott et al., 2003). Klein (2002) suggested that the audit committee is also responsible for liaising among managers, Board, and external auditors within an organisation in order to ensure free flow of information and discussions. Blue Ribbon Committee suggested that the usefulness of committee in honouring its roles and responsibilities depend, among other things, upon its composition and frequency of meeting (Millstein, 1999).

There are empirical evidences that suggest the importance of an independent audit committee in enhancing transparency in financial reporting. For example, Bull & Sharp (1989) and Kalbers & Fogarty (1993) presented the importance of setting up an audit committee, since their activities help to enhance transparency (Koh et al., 2007; Starks & Wei, 2004; Rossi & Volpin (2004). Similarly, Vafeas (2005) stated that audit committees are instituted in order to provide mechanism for fair financial reporting and good CG. In addition, Karamanou & Vafeas (2005) asserted that the rationale of the independent committee is to ensure that the interests of shareholders are properly protected and to be free from management's influence. However, different benefits of setting up independent audit committee have been stated but little has been discussed about the cost associated with it and various challenges that they encounter. Understanding of the likely challenges, may lead to better transparency and integrity.

Furthermore, there is lack of well-developed accounting and monitoring system, which affect the degree of disclosure in the Gulf countries, leaving open doors for fraud and abuses of the financial reporting and disclosure (Al Qahtani, 2005). Abdallah & Ismail

(2016) suggested that the Governments of the Gulf countries should either formulate or adopt a new international accounting standard regulation. The aim of such initiative is to eliminate barriers that may affect cross-border M&A activities by ensuring that Gulf companies' accounts are comparable, reliable and transparent. This research considers how various CG mechanisms, as seen by the relevant stakeholders who are responsible for its formation and implementation, perceive the possibility of implementing them in weak institutional environment which characterise the Gulf countries.

#### **2.4.5 Annual Disclosure**

In OECD companies are required to disclose all relevant financial information, whether good or bad, that may influence investors' decisions (Healy & Palepu, 2001). An organisation should recognise its stakeholders' information needs and how its performance is likely to impact upon them (McGee, 2009). However, previous studies are not conclusive on the link between disclosure and organisational performance. Najah & Jarboui (2013), for instance, found that there is no significant relation between disclosure and financial performance. Many authors such as Singhvi & Desai (1971); Ahmed & Courtis (1999) and Zarzeski (1996) have examined the relationship between corporate size and disclosure in different organisation annual reports and found that firm size is positively correlated to the level of disclosure. Ho & Wong (2001) found a positive relationship between disclosure and the existence of audit committee. In addition, they found that the presence of family members in the BOD is negatively related to disclosure. In addition, Nasser & Nuseibeh (2003) examined the level of disclosure and compliance in the annual reports of Saudi listed companies and found that they are highly compliant with the mandatory requirements for disclosure. Inconsistent results were found when trying to find how the level of disclosure impact on business opportunities due to differences in socio-economic and political environments between countries and organizational structures (Lee, 1999; Haniffa & Cooke, 2005). It was argued that firms with strong Boards can structure relevant strategies and policies, and are more likely to ensure higher financial transparency (Klein, 1998). However, Brickley et al. (1994) and Haniffa & Cooke (2002) argued that dual Chair of CEO may constrain Board independence and could hinder their ability to control effectively, thus, leading to lower level of disclosures and transparency. For

example, in Gulf countries, most of the firms lack transparency due to duality of position of the Chair and the CEO (Baydoun et al., 2012).

On the other hand, independent directors are more likely to enhance firms' disclosure level, therefore, support firm long-term performance (Ibrahim et al., 2003). The level of disclosure attained is correlated to the amount and quality of information provided to the investors or stakeholders. This enables the stakeholders to evaluate the company performance and then they can take informed decisions. The impact of countries regulation in terms of disclosure is important for cross-border M&A. For example, disclosure regulations can be different in different countries and may have serious implications on cross-borders M&A (Starks & Wei, 2004). Also, most Arab countries cultures restrain them from boasting about their wealth, thus leading to reluctant to disclose their financial reports (Hossain & Hammami, 2009). Saidi (2004) argued that higher level of transparency would improve the CG in the Gulf. Therefore, having a clear regulation on disclosure and how it impacts on the company performance is essential to cross-border M&A. It would be interesting thus to explore how the Gulf context influence the level of disclosure and the factors accounting for such disclosure.

#### **2.4.6 External Auditors**

There is an extensive literature on external auditing, which provides insights into the significant roles that external auditors play in helping to ensure quality CG. Effective external auditing can have a positive impact on CG, including reporting quality and firm performance (Schneider & Wilner, 1990; Fan & Wong, 2005). OECD recommends the use of guiding principles that help to authenticate and preserve financial reporting integrity. To serve the purpose, OECD mentions selection criteria, qualification, and tenure of the external auditors and states that "All listed companies are required to change their external auditors every five years" (OECD, 1999: 89).

It is argued that the financial reporting integrity is dependent upon the quality and independence of the audit committee members (Koh et al., 2007). Existing studies such

as Simunic (1984) and Becker et al. (1998) have shown evidence that having five; six or eight external auditors improve the quality of the information and increase the level of transparency.

Skinner & Srinivasan (2012) stated that high quality of financial annual audit completed by the experienced external auditors reduce errors in the result. In addition, independent auditors are more likely to enhance management decision-making process and support long-term performance of firms when obtaining an understanding of the firm's internal control and assessing risks (Ibrahim et al., 2003). Since independent auditors are not tied to the economic bonds other than audit fee with the firm (OECD, 1999), it is unclear whether there will be conflict of interest between external and internal auditors in terms of decision-making. For example, Klein (2002) and Hogan & Wilkins (2008) suggested that increasing reliance of the auditors on non-audit service fees is harmful to the desired level of independence and is incompatible with the required objectivity in an auditor's role. In Gulf countries, companies are not fully transparent in their activities and external auditors are ineffective because of lack of professional training and inadequate information made available to them on the companies' matters (AlShammari et al., 2008).

## **2.5 Corporate Legal structure in the Three Selected Gulf Countries**

### **2.5.1 Saudi Arabia**

Since Saudi Arabia is the guardian of two holy cities; Makkah and Madinah, it is considered as the protector of Islam (Zamani-Farahani & Henderson, 2010). Islam is the fundamental source of law in Saudi Arabia as King Abdulaziz, who was the founder of the Kingdom, embedded the Islamic principles as the foundation for all governance and all administrative regulations of the State drew their authority from these principles (AlRasheed, 1996). So, Saudi Arabia has a unique legal structure due to a combination

of modern concepts with a conservative outlook of traditional Islamic principles (AlRasheed, 2010). In 2006, Saudi Arabia's Capital Market Authority issued the first set of regulations on CG due to steep decline in the stock prices (Falgi, 2009). These CG focused regulations have been generally in line with the global standards. The regulations spelt out the provisions related to Rights of Shareholders, General Assembly, Disclosure and Transparency, Board of Directors (Capital Market Authority, 2006). The section on BOD is considered the most important and it includes detailed provisions related to functions of the Board, responsibilities, formation, committees, remuneration and handling of conflicts of interests of the directors in general.

There are several rules and regulations issued by other major players of CG in Saudi Arabia that support the implementation of CG system such as Saudi stock exchange (*Tadawul*) and Saudi Organisation for Certified Public Accountants (SOCPA) (AlMulhem, 1997; Lessambo, 2014). All of these have been working side by side since the adoption of CG in the country (Almajed, 2008; Ansary, 2008).

One important thing to mention about Saudi culture is that there is a strong relationship between people, as people do not usually identify with institutions but rather by social network with the people within these institutions. As a result, the individual interrelationships can be a hindrance to law enforcement as people in authority feel constrained in objectively dealing with any situation. Moreover, when it comes to applying new laws, the Saudi Government is more concerned with social stability and pays attention to the reaction of the society, which is quite conservative and traditional in its way of thinking (Vogel, 2000). Such context puts in jeopardy of implementing regulations aimed at aligning the countries' CG with some classical CG globally.

In 1926, the first *Majlis Al-Shura* (Consultative Assembly) was formed by King Abdulaziz, however its role was curtailed and most of its functions transferred to the Ministers Cabinet due to political pressure of the royal family. It was revived in 2000 by King Fahd, who decreed a new *Majlis Al-Shura* Law. It has currently a speaker plus

150 members, of whom a fifth or 30 members are women. This law has considerably strengthened and enforced the *Shariah* principles and enabled social values, justice, wider consultation *Shura* in the decision-making process (Ammoun, 2006).

Reforms are required in Saudi Arabia to improve the disclosure and transparency, which will enhance the investment climate (Henry & Springborg, 2010). The constraints on the capital markets have been relaxed to accommodate foreign investors who are not Saudi residents. Further changes in the CG environment will depend on the authorities that oversee the integration of the Saudi capital market with the other global financial markets. The main benefits of developing good CG are better reputation and easy access to international markets through M&A (Martynova & Renneboog, 2008).

### **2.5.2 Kuwait**

Kuwait gained its independence from Britain in 1961. *Shariah* based code inspired by the Maliki Islamic school of thought along with the French civil code was the main source of legislations introduced in the early eighties and though a constitutional Emirate, its political system is based on principles of democracy (Amin, 1991). Due to this, it has attracted many immigrants from neighbouring countries who contributed to the changing cultural pattern of society by introducing new customs and perceptions. Open economy associated with crude oil reserves had enabled the Government to invest in infrastructure transformational projects (Al-Shammari & Al-Sultan 2010). Kuwait had also encouraged domestic savings and attracted foreign capital investment by issuing regulations and overseeing financial reporting to protect investors (Fasano & Iqbal, 2003).

The Central Bank is the regulator of conventional and Islamic banks and the Ministry of Commerce and Industry has a unit that is responsible for regulating the insurance companies (Ali & Nisar, 2016). In 2013, The Capital Markets Authority (CMA) issued the rules and regulations, and enforced all listed companies to comply with the code of practice. The code promotes some key aspect of CG such as transparency, disclosure,

risk management and internal control. The CG code is based on the three main pillars in the society: justice, liberty and equality. It also defines the relations between employers and employees and it guarantees rights for all people whenever their rights are violated (Al-Wasmi, 2011). CMA operates under the Ministry of Finance and is responsible for supervising, licensing and monitoring companies operating in markets (Amico, 2014). It is also responsible for ensuring smooth mobilization and allocation of varied capital resources for financing strategic investments (Zeitun, 2014).

In spite of the presence of such regulatory body, the regulatory process appears to be ineffective and the CG system in Kuwait is very fragile and that is evident from transparency and disclosures by listed companies which are feeble (Al-Saidi & AlShammari, 2014). This is also seen in the fact that Kuwait was ranked the lowest among the Gulf countries, based on the level of disclosure and how the Governments encouraged professionals to avoid suspicious activities and conflict of interest (AlShammari & Al-Sultan, 2010).

### **2.5.3 UAE**

UAE gained its independence in 1971. UAE comprises of seven emirates, Abu Dhabi and Dubai are the richest among the emirates. It adopts a combination of French civil law as well as *Shariah* law. The legal structure of UAE consists of federal authorities that are united by the links of mutual destiny, history, language and religion (Al Abed, 2001). Although the core ethics of rule in UAE had been extracted from *Shariah*, early moves towards Westernisation brought into focus the conflict between Western laws and the traditional *Shariah* (SRAIRI, 2013).

The two main constituents of UAE, Dubai and Abu Dhabi have established independent free zones with their own regulations, for example, Dubai's financial free zone is known as Dubai International Financial Centre which is regulated on the basis of English law. Central bank of UAE regulates Islamic banks and Insurance Authority

regulates Islamic insurance companies in the country (Ali & Nisar, 2016). UAE made a significant progress in 2006 by establishing Hawkamah (the Institute for Corporate Governance), in order to bridge the CG gap in the Middle East and North Africa. It aims to support the Governments, regulators, companies, Boards, and other CG stakeholders to achieve higher level of transparency in the markets and promote better practices (Singh & Singh, 2010). In 2008, Mudara (the Institute of Directors) was established as a separate institution for facilitating professional development of BOD members, managers and governance professionals through education, research, information, networking and dialogue (Pierce, 2008). These institutions have helped to increase the awareness of CG among Gulf countries in general and UAE in particular to support better integration with the globe through M&A.

Ulrichsen (2011) emphasised that Gulf countries have been more prominent in the international arena in recent years, and Gulf corporations are contributing to improve CG in line with international best practice. The adopting of strong CG standards may increase the trend of M&A activities and continue integration with the global markets. However, Garabato (2009) noted that there are also some negative factors affecting M&A in gulf countries, such as low disclosure level; lack of understanding of new issues; lack of mature regulatory standards for Islamic companies. The cultural factors and religious aspects still remain an ongoing concern for the adoption of international perspective (Aribi & Gao, 2010).

Despite the similarities, both in financial and political structure among Gulf countries and the efforts that have been made to integrate their economy like the European Union, differences in their legal structure can weaken the unification of Islamic CG and pose challenges as noted by Darrat & Al-Shamsi (2005), who found UAE and Bahrain having much higher standards of CG than other countries in the region. Formulating a unified economic region required a unifying set of regulations and standards to develop the capital market. According to Hasan (2009), a strong and unified system of CG is important to ensure a strong system of co-operation among the Gulf members. Saidi (2004) also suggested that the regulators in the Gulf countries might adopt better CG



practices and learn from stronger policies from outside the region. Legal structures in Gulf countries are functions of culture, religion influences, which specify the importance of ethical principles.

## **2.6 Good Corporate Governance**

The core principles of CG are reflected in four fundamental concepts: responsibility, accountability, fairness and transparency (OECD, 1999). There are three organisations that set to improve the principles and guidelines of CG; (i) Organization for Economic Co-operation and Development Principles of Corporate Governance (OECD);(ii) World Bank and (iii) International Monetary Fund (IMF) (De Nicolo et al., 2008). However, the principles are not legally binding, but rather they were set to serve as a reference point for stock exchanges, investors, corporations and other parties that have a role in developing good CG (Nestor, 2001). Some countries failed to meet the standards due to cultural, political and religious backgrounds (O'Sullivan, 2000). OECD (1999) emphasised that good CG can be obtained through a combination of efforts between regulatory and voluntary actions. This implies that understanding and combining the differences in culture, politics, religion, regulations will help to mitigate any barrier that may affect the unification of CG principles.

There are numbers of key reasons for the need of good CG: (i) maximize firms' contributions to the overall economy;(ii) to overcome vested interest; (iii) to achieve sustained productivity growth; (iv) to mitigate the amount of risk that may involve practices such as fraud; (v) to maintain public acceptance and image; (vi) to improve company performance so as to maximise profit (Oman, 2001; Aguilera & Cuervo-cazurra, 2004). Fan et al. (2011) stated that good governance improves corporate accountability and performance simultaneously as a means of attracting human and financial resources on the best possible terms. Hope (2003, p.3) noted that "good governance in all its facets, has been demonstrated to be positively correlated with the achievement of better growth rates". Thus, it can be concluded that good CG enables

the formulation and implementation of policies, procedures and structure necessary to enhance the organisational performance.

Furthermore, World Bank has worked closely with the OECD to encourage self-assessment and evaluate companies' performance in developing countries, for the purpose of identifying strengths and weaknesses (Jesover & Kirkpatrick, 2005). This helps in enhancing the CG at the national and international level by adopting best practices and implementing legal and regulatory reforms. This is consistent with the Bank's comprehensive development framework that focuses on good governance as a key factor in effective development (Iskander et al., 1999). In addition, IMF has contributed to CG by developing codes of good practices mainly for the transparency of Governments' financial and monetary policies. The code stresses issues such as clarity of roles, responsibilities of Government and public availability of information (Vreeland, 2003). Therefore, developing a model for continuous assessments of companies' performance to identify areas of improvement is essential for good governance practices.

Good governance assures an adequate return for investors, who are beginning to show concern about the business model, which protects their investments (Bai et al., 2004). The World Bank (2006) reported that good CG decreases vulnerability of emerging market to financial crisis, reduces costs of transaction and capital cost, and reinforces rights of property which leads to development of capital market. In addition, financial reporting, auditing standards and practices are considered as a crucial part of good governance (Saidi, 2004). On the other hand, weak CG decreases confidence of investors and can discourage outside investment. Consequently, one question that might need to be asked is how to provide good CG for shareholders or investors.

Despite the proposed good CG standards and principles being acceptable in different countries, there seems to be challenges in terms of implementation and interpretation. Generally, from a cross-country perspective of CG, Claessens & Yurtoglu (2013)

observed it is not possible to have common global framework. Also, there will always be a variation in the way it is implemented and interpreted as social norms vary from one nation to the other (Licht et al., 2005). According to Lewis (2005) *Shariah* Law plays a significant role in the day-to-day aspects of life in Islamic countries. Therefore, CG may have to operate differently in Islamic countries and the conventional model may not necessarily work well in these economies where conformance with *Shariah* will need to be ensured. The next section focuses on Islamic CG.

## **2.7 Islamic Corporate Governance**

### **2.7.1 Shariah Legal Sources**

Azhar (2010) defined '*Shariah*' as the Islamic legal system or the code of law derived from *Qur'an* and *Sunnah* and a *Shariah* scholar is a person who responsible for issuing legal ruling known as *Fatwa* (plural form *Fatawa*). *Shariah* has two main sources. The primary sources are the *Qur'an* and the *Sunnah* while the secondary sources are through *Ijma*, the consensus *Fatwa* of scholars representing the will of the community, through *Qiyas*, a *Fatwa* by a scholar based on analogies from the *Qur'an* and *Sunnah* (Khoury, 2003) and through *Ijtihad*, the use of independent reasoning to find solutions to a religious question (An-Na'im, 2002).

*Shariah* law is only applicable to Muslims and under the Islamic law there is no separation of religion and state (Johnson & Vriens, 2011). *Shariah* law is divided into two Jurisprudence elements: worship and interactions. The first element *Ibadat*, refers to the five pillars of Islam and it is concerned with the person's relationship to *Allah* while *Muamalat* refers to political, social and economic interactions between entities (Warde, 2000).

#### **2.7.1.1 Primary Sources of Islamic Law**

The Holy *Qur'an* is the last revealed word of *Allah* to the Prophet Muhammad (s.a.a.w) by Angel Gabriel (Hoodbhoy, 1991). Furthermore, it is considered as the first primary

source of law in Islam that identifies all economic aspects as basis on which business community should be created (Naqvi, 2013). However, Lee & Detta (2007) argued that the *Qur'an* is not a legal document but it is a religious book based on moral principles and does not state regulations nor explicitly deal with every conceivable circumstance applicable to modern world. Therefore, *Shariah* scholars normally use the principle of *Fiqh*, jurisprudence as a methodology to interpret the *Qur'an* and *Sunnah* to offer interpretations for emerging contemporary issues (Wilson, 2008).

The second primary Islamic law source is *Sunnah* (the authentic tradition), which is derived from *Hadiths* and it is a set of sayings, deeds and reports of the Prophet Mohammad (s.a.a.w). *Hadiths* are accounts of the Prophet's life that expand on everything in the *Qur'an* (Iqbal & Llewellyn, 2002). Many verses of *Qur'an* (for example, *Al-Hashr*, 59:7) advise Muslims to take from the words, actions and life of the Prophet and abstain from doing forbidden actions. All CG principles such as transparency, justice, responsibility and accountability have been discussed in the *Sunnah* (Malekian & Daryaei, 2010).

#### ***2.7.1.2 The Secondary Sources of Islamic Law***

The first secondary source of Islamic law is the *Ijma*, a consensus opinion of scholars on certain religious issues in a certain period of time (Hasan, 1975). The process of *Ijma* is encouraged by Prophet Mohammed (s.a.a.w) as a mechanism to arrive at a unified position when two or more equally valid opinions exist among the scholars based on their interpretation of *Shariah* (An-Na'im, 2002; Philips, 2006).

The second secondary source of Islamic law is the *Qiyas* (analogical deduction) with the purpose to extend the ruling from an original case by finding a similarity between new cases and early practices. Thus, *Shariah* scholars can provide regulations for a new case based on same common grounds with an earlier case (Aldohni, 2015). Finally, *Ijtihad* is the use of independent juristic reasoning exercised within large groups of

*Shariah* scholars to issue a religious decision on issues where there is little or nothing in *Qur'an* and *Sunnah* (Al-Dihlawī & Dehlawi, 2003).

Consequently, *Ijma*, *Qiyas* and *Ijtihad* have been increasingly demanded to formulate new laws and regulations to cope with new situations and to deal with new aspects of community life (Pollard & Samers, 2007). In order to accomplish *Maqasid Al-Shariah* (intent or the purpose behind the *Shariah* rulings), these sources can form a basis for *Shariah* compliant financial investments, financial instruments as well as notions of CG for Islamic companies and it is important the *Shariah* scholars to co-operate and jointly develop better Islamic CG framework to satisfy business needs (Suleiman, 2000; Hassan & Lewis, 2007).

After Prophet Mohammed's (s.a.a.w) death, four major schools of Islamic jurisprudence had emerged and founded by the Imams; *Ibn Hanbal*, *Abu Hanifa*, *Malek* and *Shafei* at different times as well as *Jafar* who is the founder of *Shia* school of thought (al-Dihlawī & Dehlawi, 2003), while the first four are equally acceptable for *Sunni* Muslims to follow. These schools are influenced by political, social, geographical and demographical factors, which affect their orientations and application of *Shariah* (AnNa'im, 2002). This implies that different interpretation of scholars is the cause of having difficulty in defining clear rules and regulation of Islamic CG (Haqqi, 2014). For example, extremists will interpret it to suit their own agenda while moderate Muslims would offer a different interpretation, which then leads to confusion and misunderstanding of *Shariah* principles either for Muslims or non-Muslims (Goodall Jr, 2012).

To help in reaching some sort of standardisation for business practices, two organisations have been established in Malaysia. In 1990, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) was established to provide guidance for Islamic companies to follow in evaluating their practices in terms of *Shariah* compliance and to develop the *Shariah* governance framework (Abdullah &

Chee, 2010). In addition, in 2002 the Islamic Financial Services Board (IFSB) was established, and is international standard-setting organisation for the Islamic financial services industry by issuing global standards and guiding principles (Molyneux & Iqbal, 2006; Ahmad, 2010).

## **2.7.2 Principles of Islamic Finance**

### ***2.7.2.1 Prohibition of Riba***

*Riba* is an Arabic word that means addition or increase, and it occurs when the lender adds a premium along with the principal amount that must be paid by the borrower as a condition of loan after a given period of time (Algaoud & Lewis, 2007). *Riba* is one of the Islamic finance principles and according to all Muslim scholars and jurists *Riba* and interest are synonymous (Chapra, 1992).

Globally, the application of interest has been viewed differently at different times. For example, Visser (2013) noted that the prohibition of interest was not limited to Islam only; the Christian Church at various times took a strong stand against receiving or paying interest. In addition, in Judaism interest on loan was also forbidden to be applied on loans made to Jews, but it was permissible to make loans with interest to non-Jews.

In the Islamic practice, Muslims are not allowed to pay or receive interest irrespective of any reasons (Saeed, 1995). This suggests that *Shariah* prohibits a positive fixed return on a loan as a reward for waiting. For example, *Qur'an* has forbidden *Riba* in the strongest terms and its consequences in the following verses such as that in *Al-Rum* (30:39) which has meaning of increase “*And whatever you give for interest to increase within the wealth of people will not increase with Allah*”. In addition, in *Al-Baqarah* (2:278) it is mentioned that once a debt is created in any unfair dealing, any increment above the principal is prohibited “*O you who have believed, fear Allah and give up what remains due to you of interest, if you should be believers*”. Finally, Allah gave warning in *Al-Baqarah* (2:275) “*Those who consume interest cannot stand on the Day of Resurrection .... Allah has permitted trade and has forbidden interest*”. Therefore,

understanding the reason for the prohibition of *Riba* is essential for Islamic companies operating in the global market.

The rationale behind the prohibition of *Riba* is: first, *Shariah* aims at socio-economic justice and equitable distribution of resources between people in society in order to prevent wealth being concentrated in few hands (El-Ashker, 1987; Siddiqi, 2004). Second, it is considered as oppression and inequitable practice when someone is constrained to borrow money with additional amount (Naser & Moutinho, 1997). Finally, it widens the gap between people in the society by shifting the risk from lenders to borrowers when they are unable to repay (Siddiqi, 2004). However, when return is given based on profit or loss sharing, justice is achieved. This means that the Islamic finance is based on mutual sacrifice to fulfil the basic needs and develop human life (Chapra, 1992).

Ahmad (2009) argued that yet no Islamic country is fully applying *Shariah* principles as *Riba* has increasingly practiced in the Islamic world because of the serious economic dependence on the Western world (Baydoun & Willett, 2000). As a result of that, the concept of loss and profit sharing has become rare. Some *Shariah* scholars argued that since an Islamic company must interact with global business, it is difficult to conduct its business strictly in accordance with *Shariah* (Tomkins & Karim, 1987). For example, Ahmad (2009) stated that an Islamic company is allowed to charge interest at simple rates between 4% and 8%. However, this led to more exceptions and further relaxations which affect *Shariah* CG in different ways.

For this reason, Islamic companies are required to disclose transactions that involve *Riba* and provide evidences of efforts that have been taken to prevent interest practices. Kasri (2014) argued that if mimic practices of return on shares or deposits are found in the Islamic banks, then they are not purely *Shariah* compliant. However, Mohsin (1992) justifies that if the return on shares is fixed and maintained then it would not be against *Shariah* because uncertainty is not involved. Islam stands on interest is clear based on

*Qur'an* and *Sunnah*, however, how it can be practiced on the global markets where conventional practices are dominant. The question is then 'is the need for international investment and globalisation compromise the religious belief on prohibiting interest earning? Such issues are to be considered in this study.

#### **2.7.2.2 Obligation of Zakat**

*Zakat* means "purity" and is the third pillar of Islam that underlines the socio-economic development. El-Ashker (1987) defined *Zakat* as a religious tax payable by Muslims on their net worth. The objectives of *Zakat* as a tool of wealth-sharing are to ensure equal distribution of wealth, decent quality of life for poor and needy, and eradicating poverty among Muslims (Raimi et al., 2014). For instance, the recipients of *Zakat* are stated in *Qur'an* in *Al Tawbah* (9:60) "*Collected Zakat is for: the poor, the destitute, those who collect it, reconciling people's hearts, freeing slaves, those in debt, spending in the way of Allah, and travellers. An obligation imposed by Allah*". Therefore, it is obligatory for Muslims to pay *Zakat*.

Conservative scholars argued that only Islamic Governments can collect *Zakat* and some Muslim countries such as Malaysia, Saudi Arabia and Kuwait have established Government institutions that are responsible to collect *Zakat* from companies (Akhyar Adnan et al., 2009). For the management of *Zakat*, Bremer (2015) suggested that there is need to manage *Zakat* collection and distribution very effectively, since it is an obligation payment from Islamic companies. Also, Islamic companies need to increase the level of transparency and accountability to ensure purposes for which *Zakat* can be used. Therefore, it is still unclear how Islamic companies manage *Zakat* during M&A due to differences in principles and practices.

Chapra & Ahmed (2002) argued that conventional taxation system, which is implemented worldwide, is more likely to create deadweight losses which can be



minimised through the effective implementation of *Zakat*. This can prevent the losses which are caused by tax evasions because *Zakat* is fixed and room for tax evasions is very small. Further, the continuous changes in both rates and structure of the modern taxation system leads to greater losses as most businesses fail to understand and adjust their business plans according to these changes whereas the system of *Zakat* is simple and fixed and there are no changes in terms of rate and structure (Archer & Karim, 2002).

However, the question is, would it be possible to create enabling environment in the modern world for accepting *Zakat* based on their differences in moral and social values. Hasan (2010) claimed that imposing *Zakat* globally will overlap with the current international taxation system and will lead to discrimination and shift equity investors' preference to the conventional banks. Similarly, Garas & Manama (2007) argued that *Zakat* creates double taxation in international deals because of the dual regulators (Islamic and conventional). Therefore, *Zakat* has great importance especially in cross-border M&A and it needs to be considered before forming the deals.

#### **2.7.2.3 Islamic Inheritance Law**

*Mirath* is the Arabic word of succession, and it is a fixed share, of all property held by the deceased, allocated to various blood relatives who are clearly stated in *Qur'an* and *Sunnah* and give specific details of inheritance shares (Mohd Noor & Abdullah, 2009). *Shariah* clearly defines the law of inheritance based on composition and gender of family members. The distribution of *Mirath* must be after payment of legacies and debt of the deceased (Hussain, 2005). *Qur'an* mentions nine obligatory inheritors; mother, father, husband, widow, daughter, uterine brother, full sister, uterine sister and consanguine sister. *Shariah* scholars have added a further three inheritors by applying the method of *Qiyas*; paternal grandfather, maternal grandmother and agnatic granddaughter (Zuleika & Desintha, 2014).

There are primary and secondary successors that are entitled to a share of the inheritance in Islam and the division of inheritance is a separate subject with huge details (see Appendix 1). The inheritors with specific details of shares are stated in the *Qur'an* in *Al-Nisa* (4:11, 12, and 167). The Islamic inheritance law, under which the business is transferable to the closest blood relations of the business owner, is quite a complex matter based on the relatively large family size in Gulf countries (Hamadeh et al., 2008). Therefore, deeper understanding of the Islamic inheritance law is important for successful implementation of cross-border M&A between Islamic and non-Islamic companies.

## **2.8 Philosophical Foundations of Islamic Corporate Governance**

Understanding the role of religion in the greater context within a society is important to determine the guiding principles behind CG in any religious society. Licht et al. (2005) argued that seeking religious guidance on CG appears needless because CG issues need public considerations whereas religion is a personal affair (Lake, 2010). However, this argument does not stand up when considering the role of religion in influencing people's behaviour and organizing human life (Zein et al., 2008; Lelkes, 2006). When the religious beliefs are deeply held by a large section of society, they influence all interactions and transactions and therefore cannot be ignored as personal belief.

Kettell (2011) Wilson (1997) have observed, most religions are from the same source and most religions highlight similar principles such as transparency, responsibility, accountability, trust and these concepts provide a foundation for good governance.

There are religious principles that strongly encourage individuals to always fulfil their responsibilities, promises and contracts, for example, Ali & Weir (2005) explained that Islamic ethics in *Qur'an* are virtue and they establish harmony and equilibrium in a person's life. It is stated in *Qur'an* in *Al-Maidah* (5:1) "*O Ye who believe, fulfil your undertakings*".

Islam is not a new religion but rather the continuation and comprehension of previous religions (Alsheha, 2012). Islam regards itself as the perfection of the previous religions, Judaism and Christianity (Ezzati, 2002). Although *Qur'an* clearly states that Muslims believe in the earlier revelations (Religions), however the practices of preceding religions have been corrupted over period of time. In fact, the most obvious example of such corruption is ascribing divinity to Jesus (Stark, 2003). For this reason and others, Islam provides guidelines and rules that cover all aspects of life and followers should practice them and reflect upon in their actions (Vogel & Hayes, 1998; Al-Zuhayli, 2005; Dusuki, 2008).

Muslims' central belief is the building block of *Tawhid*, the concept of indivisible oneness of God. God always exists and creates everything in the world (Schuon, 2003). Thus, Muslims believe that they obtained direct teaching from *Allah*, which provides absolute guidance to humans (Haron & Nursufiza, 2008) and by fulfilling these, people will contribute positively to society (Zein et al., 2008). Furthermore, God has not left any one empty-handed to fulfil his or her responsibilities but rather God provides physical and intellectual capabilities, knowledge and other resources (Hassan, 1982).

However, Abuznaid (2009) argued that every individual is free to choose between an ethical life and a life motivated by self-interest. A'laMawdudi (2001) discussed about the challenges in changing people's behaviour to the norms of a particular religion so that they can contribute to the growth of the society. In the contemporary society, one of the main challenges that Muslims encounter is in the development of a socio-cultural and political-economic framework that reflects Islamic principles (Norris & Inglehart, 2012). However, there has been no remarkable progress till date due to the complexity involved in restructuring a modern conception to conform to Islamic principles, which allow mechanisms for consensus building but by implication allows space for different interpretation except in case of specific prohibitions.

CG is a contemporary concept; however, its fundamental principles are already reflected in the *Qur'an* and *Sunnah* (Hassan, 2009; Hassan & Lewis, 2009). It is also essential to understand that *Maqasid Al-Shariah* or the purpose or rationale of *Shariah* encompasses the basic concepts of *Amanah* (trust), *Adalah* (justice) and *Shura* (consultation) and these can readily contribute to the development of Islamic theory of CG (Dusuki & Abdullah, 2007; Chapra et al., 2008). At conceptual level, the concept of CG for both the Islamic and non-Islamic companies can easily benefit from these principles, if implemented properly (Rahman, 1998). However, it is difficult to define an Islamic CG framework that is uniformly acceptable to a diverse range of *Shariah* scholars, who might draw their inspirations from different aspects of the *Qur'an* and *Sunnah*, depending on their experience and outlook. Therefore, how such understanding and interpretation of *Qur'an* and *Sunnah* manifest out in the three countries under study. Do they exhibit similarity or difference?

## **2.9 Islamization of Knowledge**

Some three decades earlier, Islamization had been introduced as a term to refer to integration of Muslim's principles, ethics and morals into the modern knowledge to reinforce their religious identity (Kartanegara, 2007). Hashim & Rossidy (2000) mentioned that the two main proponents, who used the concept of Islamization of knowledge (IOK) were: Al-Attas (1978) who introduced this concept in his book "Islam and Secularism"; and Al-Faruqi (1988) in his book "Islamization of knowledge: problems, principles, and prospective". Al-Faruqi (1988) defined IOK as integrating the new knowledge into the Islamic stream by re-interpreting and adapting its principles into the new concepts, while Siddiqi (1989) linked the IOK with the movement to restore Islam's position in the contemporary society.

Contemporary knowledge in Islamic society, therefore, is not obtained directly and solely from Islam itself, but it needs to be reframed in order to be make it Islamic (Ibrahim, 2014). Salleh (2011) stated that Muslims derived their ethics from *Qur'an* and *Sunnah* whereas ethics in Western theory, though derived from secular social values, have nevertheless Judaeo-Christian influence. The concept of IOK came as a reaction to

the failures of both the Capitalist and Socialist systems as there was disconnect with the social reality and even violation of ethics in Muslim societies (Tibi, 1995). Consequently, there were greater calls from Muslim world to revive their ethical standards and for Islamic scholars to create Islamic solutions (Haneef, 2005). To date this issue has been cardinal for discussion in various international conferences.

Al-Faruqi (1982) developed Work Plan to revive the methods of early Muslim philosophy, and restore *Ijtihad*. Moreover, Daud (2009) emphasised that Muslims need *Ijtihad* to apply the old dictum on the new situations and to establish the specific relevance of Islam to each area of modern knowledge. Ai (2010) observed that it is important to make efforts in the case of the Islamization of conventional CG model. However, al-Faruqi (1998) pointed out that it is not an easy task to reframe new knowledge to ensure compliance with *Shariah*. Nasr (1992) observed that the process of Islamization of knowledge might emerge to secular intellectual as a set of guidelines without any violations of the *Shariah* principle.

Al-Attas (1978) argued that IOK is the logical consequence which seems to be a response to Secularization or Westernization. Therefore, the process of IOK is governed by *Qur'an* and *Sunnah* through *Tafseer* and *Ta'wil* (explanation and interpretation) as valid Islamic methods of gaining knowledge. Islam always encourage individuals to discover the truth but within the boundaries of *Shariah*.

## **2.10 Spirit and Letter of *Shariah* Principles**

In order to comply with rules and regulations, it is important to understand the concepts of 'letter of the law' and 'spirit of the law' (Choudhury & Hoque, 2006). The letter of the *Shariah* law is defined as formal principles, code, rules and regulations that must be followed by an Islamic society, while the spirit of *Shariah* law is that Muslims should not only obey *Shariah* principles but also comply with the intention behind it (Chapra & Ahmed, 2002; Archer & Karim, 2002).

According to Al-Shamsi (2005), the social consensus on the interpretation of *Shariah* principles cannot be developed unless the society is aware of them. Mawdudi (1976) noted that interpretation of letter of *Shariah* law can be different in different Islamic societies. Thus, the *Shariah* scholars' *Fatawa* can be different according to the given circumstances. Understanding on how to balance the different interpretation among the Islamic countries can be challenging due to cultural differences and *Shariah* scholar perceptions. This begs a question about the subjective nature of interpretations by *Shariah* scholars which could be different from scholar to scholar and to what extent such difference in interpretations influence the effectiveness of the Islamic CG in the context of cross-border M&A. The answer to this question has also implications for the CG structure and mechanisms.

The compliance with *Shariah* law can be done effectively when the business leaders and *Shariah* Board members understand spirit and letter of *Shariah* law which focuses on protecting the interest of the people living within the society (Aggarwal & Yousef, 2000). Understanding spirit and letter of CG principles from an Islamic perspective could be critical for any business, as it would be helpful in providing guidelines, enhancing the financial liquidity and minimising the business-related risks (Akkizidis & Khandelwal, 2007; Ahmed, 2009). For example, Shirazi & Amin (2010) noted that *Zakat* is obliged to create giving culture that could boost Muslims materialistically in the eyes of other communities, and spiritually in the eyes of *Allah*. Therefore, wellbeing of Muslims' community relies heavily on individuals' behaviour (Zaman et al., 2013). King (2007) identified that Muslims are answerable and accountable to *Allah*, as moral and spiritual facets are considered the core of Islamic CG particularly in the decision-making process.

## **2.11 Development of Islamic Finance in the Gulf Region**

At the end of 2012, Islamic finance has expanded its operation in more than 50 countries and the volume of assets under Islamic finance reached a growth of between 15 to 20% per annum (Yaacob & Donglah, 2012). Middle East is the centre of Islamic

finance with contribution of approximately 74% while 26% share is contributed by the rest of the world (Hanif, 2014).

The Islamic Financial Services Board (2015) reported that the Islamic finance industry has attracted investors worldwide, which has led to increase in its business and economic activities both regionally and globally. Also, they reported that the evidence was attributed to its double-digit compound annual growth rate of 17% between 2009 and 2013. In addition, the industry's assets are estimated to be worth USD1.87 trillion as at 1<sup>st</sup> Half of 2014, having grown from USD1.79 trillion as at end-2013. The Gulf region accounts for 37.6% of the industry assets, and a market value of US\$ 564.2 billion of the total global Islamic financial assets. This was attributed to the positive impact of the *Shariah* law principles on Islamic banks' economic activities and on society as a whole (Sairally, 2007; Mansoor & Ishaq, 2008).

Historically, Islamic banking has been originated in the Gulf countries since the Dubai Islamic Bank was set up in 1975 (Zaher & Kabir, 2001). Bahrain, Qatar and lastly Saudi Arabia launched their Islamic banks in 1979, 1982 and 1987 respectively. Saudi Arabia supported the international Islamic finance initiatives by establishing the Islamic Development Bank in Jeddah (Islam & Kamruzzaman, 2015). This was expected to positively influence the attitude of the Saudi authorities to Islamic banking; however, they remained surprisingly cautious (Wilson, 2009). Similarly, in 1977 Kuwait established Kuwait Finance House (KFH). GCC Islamic banks such as Al-Rajhi bank in Saudi Arabia and KFH in Kuwait have been expanding globally in Turkey, Malaysia, Singapore and Melbourne. In addition, Dubai Islamic bank is taking a rapid global perspective and has invested in Pakistan, Turkey and United Kingdom (Parashar, 2010; Ahmed, 2010; Wilson, 2013). Jbili et al. (1997) argued that the Islamic banks in Gulf countries are well developed and profitable in the region as they hold high levels of capital; which has enabled the banks to endure the global financial crisis.

However, banks in the Gulf are relatively small and that might limit their activities domestically and internationally (Hassan et al., 2010). Further, Al-Muharrami et al

(2006) argued that Gulf banks need to merge together to be able to compete and survive internationally when they expand their business globally. Thus, adopting good CG code is essential for Islamic banks in which they plan to transform their economies into international scene. By doing so, Gulf countries would be prepared to face opportunities and challenges of cross-border M&A (Saidi & Kumar, 2008; Al-Musalli & Ismail, 2012; Zeitun, 2014). Nevertheless, Obaidullah (2005) and Ayub (2009) argued that Islamic financial system is less developed in comparison with conventional financial system and it is still at an early stage of evolution as many problems must be addressed relating to theories, practices and a slow pace of innovation of Islamic financial instruments. Due to the absence these, conventional banking continues to exist in the Gulf region (Wilson, 2009).

## **2.12 The Islamic CG Model**

Considering the size of Islamic finance, very little attention has been given to Islamic CG. Islamic financial institutions have been criticized for the lack of accountability and transparency especially after seven suspects who reportedly swindled \$501 million involved Dubai Islamic Bank in 2009 (Za'za, 2009).

There is not even as yet a unified definition of Islamic CG, Elasrag (2014) defined Islamic CG as a system by which firms are controlled and directed with a purpose to attain the objective of corporation by protecting the interests of all stakeholders. Islamic CG sets out the corporate structure, its process as well as administration to ensure that all transactions are in accordance to *Shariah* (Safieddine, 2009). It helps to recognize that the practices conform to *Shariah* in terms of both letter and spirit of the law (Akhtar, 2006).

Choudhury & Hoque (2006) and Farook & Farooq (2011) argued that Islamic companies' structure is complicated than those of conventional corporations due to religious and cultural factors that are involved in shaping Islamic CG, and therefore there is need to analyse and scrutinize Islamic CG by stakeholders across the industry



for more robust CG framework. Faiz (2011) argued that CG practices of Islamic companies around the world are diverging due to a non-prescriptive approach of the regulators.

Islamic perspective of CG comes from Islamic epistemology to premise on the divine oneness of God and it supports the achievement of corporate goal without ignoring the duty of social welfare (Choudhury & Alam, 2013). It is a stakeholder-oriented model which takes a wider theory of decision-making to protect the rights of all stakeholders who are exposed to any risk as a result of the firm's activities (Molyneux & Iqbal, 2006). However, Beckett (2003) and Hasan (2009) and argued that most Islamic financial institutions adopt Anglo-Saxon model, this is due to the fact that majority of Muslims' economic activities are inherited from the Western colonial powers. Chapra & Ahmed (2002) argued that, unlike the conventional companies, the depositors rather than shareholders in Islamic companies provide a large proportion of funds and this provide a completely different CG structure. Islamic banks pay depositors based on the bank profitability (Ariff & Iqbal, 2011), thus the Islamic depositors are exposed to greater risks based on profit and loss sharing and equity based contracts (Safieddine, 2009; AlSuhaibani & Naifar, 2014). All properties are subject to *Shariah* law, and the right to enjoy a property should be balanced between all stakeholders (Iqbal & Mirakhor, 2004).

There are also additional important differences in terms of enforcement, for example, Hasan & Dridi (2010) argued that any change in CG model in the case of Islamic perspective could be very difficult to achieve because the related laws and regulations are defined by God. However, in conventional perspective, the desired quality of CG is enforced through introduction of new laws and regulations. In the case of Islamic CG, it only requires an interpretation of the existing laws in the specific context of the corporation and business environment. CG involves a very high degree of subjective decision-making and judgement from the Islamic perspective (Al-Gamal, 2006; AbuTapanjeh, 2009). Vinnicombe (2010) argued that Islamic companies show high levels of compliance with *Shariah* in some respects, while low level of compliance in

others such as disclosure of *Zakat* due to the conflict of interest between the parties involved. Therefore, understanding these differences based on global market are essential for easier business integration.

### **2.13 Shariah Supervisory Board**

In 1999, AAOIFI standards have defined *Shariah* Supervisory Boards' (SSB) roles and have provided guiding principles for Islamic financial institutions. The Board structure of Islamic CG adds an additional Board; this implies two Boards namely BOD and SSB (Hasan & LAWS, 2007). SSB is a committee consisting of a group of Islamic scholars who are specialist in the field of Islamic jurisprudence *Fiqh Al-Muamalat*. However, considering the complexity of Islamic business transactions, members of SSB should be familiar with both Islamic law and modern financial needs (Rammal & Parker, 2010). They should be no less than three members, whose primarily act as an advisory Board that direct, review and supervise Islamic companies' activities (Grassa, 2013). The selection of SSB members should be done through the shareholders annual general meeting based on the recommendation of BOD (Paino et al., 2011).

SSB is one of the vital elements to promote the growth and stability of the Islamic finance. In addition, SSB ensures the Islamic companies are operating in conformity with *Shariah* principles and it increases the credibility of the institutions in the eyes all stakeholders. SSB members have a great role on the day-to-day practice and on the development of new procedures and products (Grais & Pellegrini, 2006). SSB members can be from internal or external sources and they receive salary or payments based on meetings attended and they have the right to be appointed in other SSB of different companies. However, Lewis & Algoud (2001) argued that maintaining internal SSB members is better to help in understanding and assessing their individual organisations, thus improving the overall environment.

In the absence of a well conceptualized Islamic CG framework, practices of Islamic companies differ based on different countries' jurisdictions and regulations. While it can create additional agency problem and conflict of interest, the external SSB members provide a mechanism for sharing the understanding of critical issues and possible solutions. Therefore, understanding all sides of arguments and their impact is important to enhance the Islamic CG model (Moudud, 2015).

## **2.14 Islamic Financial Instruments**

Islamic finance market offers various products to satisfy providers and users of funds in various ways. The number of *Shariah* compliant products is growing as Islamic finance is expanding globally (Wilson, 1991). Islamic mode of finance is based on prohibition of *Riba* and there are three main categories which are the building blocks for developing a wide range of more complex products. These three modes are based on Partnership (profit and loss sharing), Trade, and Rent (El Qorchi, 2005). The use of each mode is based on the purpose and size of transactions. In addition, there are other Islamic financial instruments such as *Sukuk* and *Tawarruq*. This suggests that Islamic financial markets have seen financial innovations and global expansions (Iqbal, 1999).

Although Islamic banks have attracted deposits from Muslims around the world, there is lack of skill or ability of Islamic institutions to invest efficiently. In addition, conventional banks offer Islamic channels of investments; however, some of them are not acceptable from a strict *Shariah* point of view (Iqbal, 1997). Identifying non-*Shariah* compliant products is relevant in integrating Islamic and conventional companies.

Based on Islamic principles, what actually transacts between the bank and the customer is a commodity (Khan, 2010). It is prohibited for customer to access direct cash loan from the bank. Rather, the bank purchases the item for the customer and resells it to the customer. Understanding how this practice can be integrated with the conventional

practice is essential to develop better integration policies on how different financial instruments work. However, some *Shariah* scholars have questioned such practices as they might have some element of trickeries to circumvent the prohibition of *Riba* (Amin et al., 2011).

Islamic principles require filtration process to select appropriate types of equity shares (Musa & Obadi, 2009). This is to ensure that the financial product, operation, and capital structure of each business are within *Shariah* borders. However, this process creates problems in integration with the global market as many corporations are connected with some form of prohibited activities such as alcohol, gambling and some forms of public entertainment as well as prevalence of debt financing based capital structure (Ismail, 2005; Dusuki, 2008).

#### **2.14.1 Partnership Financing Mode**

The first type of Islamic mode of finance provides direct finance as capital based on partnership (Usmani & TaqiUsmani, 2002). The basic instruments for profit and loss sharing transactions in foreign trade financing are *Mudarabah* (profit-sharing) and *Musharakah* (partnership) which provide equitable sharing of risks and profits between all parties (Dusuki, 2009; Gait & Worthington, 2007) as explained below.

*Mudarabah* refers to a contract between two parties, the investor (*Rab-Almal*) who provides the capital needed and the entrepreneur (*Mudarib*) who offers labour and expertise with the objective of making and sharing profit (Gafoor, 2001; Rammal, 2003; Jedidia & Hamza, 2014). In order to conduct *Mudarabah* contract between parties, the entrepreneur must have full control over the business; supervision is permitted by the investing bank, which shares a percentage of the profit, not a lump sum payment (Iqbal & Llewellyn, 2002).

If profits are made, the profit from the project is to be shared between the investor and the entrepreneur according to the mutually agreed ratios (Dhumale & Sapcanin, 1999).

On the other hand, if the entrepreneur made loss all parties jointly absorb the losses, by the investor losing in terms of money and the entrepreneur losing in terms of time and effort spent on the project. However, the entrepreneur is expected to work with diligence to avoid any unnecessary losses and any negligence or misconduct by the *Mudarib* may be liable for the financial losses (El-Qorchi, 2005).

*Musharakah* (partnership or joint venture) is an equity-based contract between a bank and its customers in which the bank is not the only provider of funds (Iqbal & Khan, 2005). *Musharakah* offers a significant alternative to the interest-based financial instruments found in conventional banks (El-Gamal, 2000). It has been used to finance medium- and long-term investments where two or more partners may provide the capital, and share profits. If the profit is generated or loss is made, they are shared based on each party's ratio of participation in the financing of the project (Rosly, 2005; Venardos, 2005). However, the parties may agree to share the profit on the basis of a pre-agreed ratio, for example, in case of *Musharakah Mutanakisah* (diminishing partnership), where the customer (the partner of the bank) eventually becomes the complete and sole owner of the investment for which the bank has provided the funds during the initial stages of the contract (Shanmugam & Zahari, 2009). However, losses will be shared on the basis of equity participation (Dusuki, 2009).

Each party has a right but not an obligation to participate in managing the project or to waive such right. Firms have exploited this business opportunities available in Gulf countries through formal agreement like *Musharakah* (Gait & Worthington, 2007). This has led different parties with common interest in the region to come together through the principles of *Musharakah* to invest together in different countries. However, there is little information on how to integrate or partner with non-Islamic partners. Providing a clear practice on how to partner with non-Islamic companies or individual is relevant in achieving globalisation.

It is argued that since the inception of the theory of Islam and its advancement into Islamic finance, several scholars have praised *Musharakah* and *Mudarabah* because

they present ideal forms of acceptable contracts in Islamic finance (Usmani & TaqiUsmani, 2002). Both have the capability of pooling resources as well as expertise from different potential partners (Akgunduz, 2009). Therefore, assessing their impact to the global market is essential for better integration.

#### **2.14.2 Trade Financing Mode**

The most commonly used instruments for short-term financing based is *Murabahah* (El Qorchi, 2005). It is also termed as corporate asset support or cost plus financing (Mirakhor & Zaidi, 2007). In this mode, there is an agreement between a bank and the borrower to purchase goods or import commodities on behalf of the borrower and then sell it to the borrower at agreed mark-up profit (Yousef, 2004). In this type of contracts the borrower is given a choice to either to pay in one lump sum or by instalments (Ismal, 2009). Several *Shariah* scholars have approved the use of *Murabahah* as a financial instrument to be *Halal* (Mansoor & Ishaq, 2008; Ali, 2004). However, some authors have criticised *Murabahah*, for example, Usmani (2013) has argued that it is not a real Islamic financial instrument, rather it is just a device to escape from interest and the mark-up can be excessive. The author also argued that *Murabahah* should only be considered if *Mudarabah* and *Musharakah* are not applicable.

There is risk associated with *Murabahah* due to the time of purchase and time of sale of the goods (Thomas et al., 2005). For example, the instruction made by borrower to the bank to purchase a good does not oblige it to perform immediately; the bank may delay or decide not to deliver the goods due to uncertainty. However, to mitigate such eventuality, the *Shariah* scholars have emphasised that all parties must agree on all features of the service or property to avoid future conflicts (Hassan & Lewis, 2007; Jaffer et al., 2012).

### 2.14.3 Rental Financing Mode

The most commonly used instrument among all Islamic instruments is *Ijarah* which means provide something on rent. Usmani (2006: p.2) defined *Ijarah* as “to transfer the usufruct of a particular property to another person in exchange for a rent claimed from him”. Shariff & Rahman (2003) defined it as leasing agreement between a bank and its customer whereby the banks purchases an asset such as home or car for the customer and then hands it over to the customer on rental basis. Some scholars argued that *Ijarah* is a business activity rather than original Islamic finance mode where both Islamic and conventional banks use this kind of contracts (Ahmed, 1990; Usmani, 2006). However, Islamic banks used it instead of long term lending on the basis of interest and the difference between *Ijarah* and leasing agreement in conventional system is that *Ijarah* can be *Shariah* compliant. For example, for *Ijarah* to be *Shariah* compliant all parties must agree in advance on the rent whether fixed or variable as well as the rent must be charged after the delivery of the asset, and not from the day of the payment (Ghuddah, 1998).

### 2.14.4 Sukuk

The international market for *Sukuk* “a non-interest bearing investment” has grown tremendously in recent years within Muslims countries in terms of volume and value (Wilson, 2008). It is also evolving into the cross-border market of the issuing countries such as Malaysia, Bahrain, Qatar, Pakistan, Indonesia, the UAE and Saudi Arabia (Aloui et al., 2015). In 2000, Malaysia was the first in issuing *Sukuk* (Mohamed et al., 2015), and according to Abu Sneineh (2016) Malaysia remained the largest *Sukuk* market until the first half of 2014, with a share of more than 43% and recently Gulf countries have dominated the market as Dubai Islamic Bank, the oldest Islamic commercial bank in the world, is currently the third-largest venue for *Sukuk* listings globally with a stellar 43% market share, followed by Saudi Arabia with 21%, compared to only 7% for Malaysia.

According to Global Islamic Economy Report 2015/16, Islamic Banks managed \$1.814 trillion of assets as of 2014, and there is a potential to rise to \$3.247 trillion by 2020. The increasing pattern of *Sukuk* market is due to the desire to establish a benchmark rather than simple funding requirements and encouragement of a corporate *Sukuk* development (Aloui et al., 2015). *Sukuk* refer to securities, notes, papers, or certificates with features of liquidity and tradability (Usmani, 2007). *Sukuk* are issued for a fixed time period and can vary from three months to ten years and can take various forms and structures which depend on the underlying *Shariah* principle such as *Musharakah*, *Mudharabah*, *Murabahah* and *Ijarah* as discussed earlier (Aquil, 2005).

*Musharakah Sukuk* can be structured in different ways, such as business plan, where the originator and trustee combine their resources and effort and co-ownership or where the originator and trustee contribute cash to buy and assist (Abdel-Khaleq & Crosby, 2009). *Mudharabah Sukuk* is structured in such a way that a certificate of *Sukuk* represents ownership unit value or activities managed in the project. *Murabahah Sukuk* carries equal value, for example; the bank procures a commodity and issues it to a client at a known pre-agreed profit with the intention that the client will fulfil the differed payment obligation (Wilson, 2008). Furthermore, *Ijarah Sukuk* is a certificate issued by the owner as equal value of an existing asset for the purpose of leasing it against some rental proceeds either through the owner or intermediary. The profit from *Sukuk* streams from a sale, a rental or a combination of the two (Tariq, 2004).

*Sukuk* offers the opportunity for companies to obtain fund to provide resources compatible with *Shariah* Law (Al-Amine, 2008). In principle, it is wrong to refer to *Sukuk* as Islamic bonds, *Sukuk* has advantage over conventional bonds, as it must be backed by a tangible asset such as a piece of land or building. In this case, when investors buy or sell *Sukuk*, they are not only trading the paper but also indirectly trading their real assets (Agha & Grainger, 2009; Afshar, 2013). A further advantage could be in terms of cost as argued by Vizcaino (2014), who found that the issuance of *Sukuk* could be more expensive for corporate than conventional bonds. *Sukuk* is a nascent product and it is important to develop *Sukuk* structure to suit the global market



and to facilitate legal and regulatory framework when issuing *Sukuk* outside of Islamic markets (Jobst et al., 2008).

#### **2.14.5 Tawarruq**

Literally, *Tawarruq* is derived from the word *Al-Warq* which means money and it is developed to facilitate Islamic economic activities (Khayat, 2009). *Tawarruq* consists of two transactions; first, a buyer purchases a commodity from a seller or a bank on a deferred and a “cost plus” basis, and the second buyer sells the same commodity to a third party on a cash basis (Kahf, 2004; Ahmad et al., 2009). This scenario is called *reversed Murabahah* as the buyer has a contract for a *Murabahah*, and the same transaction is reversed in the second transaction. Furthermore, this is a “cost plus” as after gaining cash from the second transaction, the buyer pays the original seller on a deferred or cash basis (Siddiqi, 2007; Nasrun, 2014). This mode of Islamic finance contracts is rapid and fixable way of gaining cash (Roudini & Karimzadeh, 2012).

Understanding the application of *Tawarruq* and its effects to non-Islamic company is relevant for an Islamic company to expand globally.

There are three types of *Tawarruq* including; real *Tawarruq*, organised *Tawarruq* and reversed *Tawarruq* (Msatfa, 2011). For organised *Tawarruq* the customer does not receive the commodity, and does not engage in the selling of it, while real *Tawarruq* the customer takes possession of the commodity for himself and can also resell it to a third party. For reversed *Tawarruq*, the bank buys the commodity and also acts as a client as well (Dabu, 2007; Msatfa, 2011). However, many *Shariah* scholars perceive some of these practices as against to the Islamic principles and the financial markets still witness some level of inconsistencies from practices in one region to another (Khayat, 2009; Kahf, 2006).

Msatfa (2011) and Mahmood & Khatun (2013) argued that *Tawarruq* creates confusion, as some scholars consider *Tawarruq* transactions as permissible while others argue that it is impermissible because it creates a charge which is similar to interest on cash loan which is *Riba* and prohibited under *Shariah* (Khayat, 2009; Iqbal & Mirakhor, 2011). Despite this argument, many Islamic banks use *Tawarruq*, including the UAE Islamic Bank and Bank Muaamalat of Malaysia (Baba, 2007). Therefore, it will be relevant to understand what rationale is used to justify the use of *Tawarruq*, as all mode of financing must be based on prohibition of *Riba*.

## **2.15 Theoretical Framework**

This section presents the theories relating to CG that are used to carry out an investigation of the impact of *Shariah* CG on cross-border M&A. Researchers such as Flak, & Rose (2005); Duhnfort et al. (2008) and Yusoff & Alhaji (2012) have suggested that sticking to one theory is not sufficient to understand CG practices and they emphasised that combining two or more theories help to provide better understanding of CG practices. For this reason, three theories were examined namely: Stewardship theory; Agency theory; and Stakeholders' theory to bridge the gap between Islamic and conventional CG practices on the factors that might affect cross-border M&A and establishing a link between theories to build a framework for this study.

### **2.15.1 Stewardship Theory**

Stewardship theory is an idealistic theory as it has its roots in psychology and sociology, and it is a substitute model of managerial behaviour (Clark, 2004). This theory suggests that the business executives are seen as stewards, who are not motivated by individual goals; however, they are motivated to serve the principal's interests (Albrecht et al. 2004; Van Slyke, 2007). Donaldson & Davis (1990) were willing to bring in a new theoretical framework to the CG, thus, they completed an empirical study against the agency theory, which is discussed later. Muth & Donaldson (1998) highlighted that Stewardship is an alternative view of agency theory. Moreover, it

shows a collective not individualistic behaviour (Davis et al., 1997). In addition, this theory claims that if there was any conflict of interest between the principals and the stewards, and if they cannot solve the problem, the stewards would prefer the solution that is in the principal's interest (Eddleston & Kellermanns, 2007).

In the same vein, Block (1993) argued that managers believe that when they satisfy the owners' interests, their benefits will be more than if they favoured their individual interests and hence there is no conflict of interest and no need for separation of duties. However, Donaldson & Davis (1990) examined a combined Chair/CEO structure of senior management and found that there is weak evidence from stewardship theory perspective that dual role has any significant impact on investors' return.

Albrecht et al. (2004) argued from a different perspective that the managers will increase shareholders' wealth as they understand the business well. Due to such assumptions underpinning this theory, this theory suggests less cost of governance since it neither requires incentives for the executives nor costs for monitoring managers (Pastoriza & Ariño, 2008).

Choo & Tan (2007) observed that although managers are motivated to act in the best interest of the principals, it is essential to address the question of to what extent they are willing to attain a good corporate performance. Moreover, Albrecht et al. (2004) claimed that stewards, based on their own moral conduct may put trust in managers and may provide opportunities to commit fraud. One of the critiques of this theory, according to Arthurs & Busenitz (2003) and Hendry (2005) is that even when goals are aligned, stewardship theory provides little help in shedding more light on as it is very difficult for individual to turn off their self-interest. In addition, Lin (2016) criticised this theory, as it is invalid in the real world since emotional human behaviour is not a valid assumption for any theory.

This research examines stewardship theory in the context of cross-border M&A in terms of compliance for disclosure, transparency and managerial behaviour. Bhatti & Bhatti,

(2009) noted that the integration of various mechanisms and the ethical issues of business are important to attract the confidence of both local and foreign stakeholders. Islamic organisations, which are operating under *Shariah*, perceive the best interest of the group rather than the individuals. This suggests that managers are motivated to perform their duties in the right attitude of partnership to comply with the Islamic values and beliefs (Sulaiman, 2005; Bhatti & Bhatti, 2009). Islam considers that individuals are accountable to God and man, thus the concept of *Khilafah*, brotherhood and *Tawhid* constitute the foundation of stewardship theory (Sulaiman et al, 2015). Prophet Mohammed (s.a.a.w) stated in his *Hadith* “each of you is a guardian and each guardian is accountable to anything under his care” (Al-Bukhari, 1986). As discussed in other sections above, there were evidences which point to the fact *Shariah* scholars and SSB could collide with the interests of the principals and this thesis sets to explore to what extent the respondents perceive these agents playing their roles in promoting the interests of the companies.

Lahsasna & Hassan (2011) emphasised that Islamic companies enjoin in collective decision making through the *Shuratic* mechanism between SSB and BOD members to ensure that the purpose of achieving all stakeholders’ interests. The level of expertise and competence of the *Shariah* Board are relevant to ensure all the companies’ services and financial products are aligned with *Shariah* (Khan, 2007; Yaacob & Donglah, 2012). Thus, could the SSB and BOD be considered as stewards of the merged companies in the Gulf context? This study sets out to find if this is the case or not.

Common distinctions between agency theory and stewardship theory, which lie in several factors such as motivation, identification and use of power, are presented by Clark (2004). There is no best way of using agency or stewardship theory alone; however, stewardship can be seen as complementing agency theory to in examining CG (YanLam & & Kam Lee, 2008). The agency theory is discussed below.

## 2.15.2 Agency Theory

The existence of a firm is characterised by the separation between the control of a corporation and its owner (Fama & Jensen, 1983). Separating ownership from control gives rise to agency problems, which have been widely discussed by accounting, economics and finance scholars in different research areas (Clark, 2004). It was suggested by Alchian & Demsetz (1972) and further developed by Jensen & Meckling (1976) based on Adam Smith's observation that it is unclear whether managers will anxiously watch over the company just like the owners. The CG concept has been emerging from the desire to describe the relationships within organizations to cater to frequent incidence of agency theory (Carlos & Nicholas, 1990). Primarily, this theory explains the relationship between the owners or principals of the company and the management who are given authority by the owners to perform work on their behalf (ICAEW, 2005). The agency problem arises when managers are not accountable for the risks associated with their decisions as well as when they act in their personal interest to maximize their own wealth (Fama, 1980; AryeBebchuk & Fried, 2003). This suggests that there is always conflict of interest between the principals and the agents (Hill & Jones, 1992; Obid & Naysary, 2014).

Opportunism is possible when opportunistic individuals can exploit the circumstances. In this connection, Podrug et al. (2010) stated that control mechanisms are important to control managers' behaviour; however, control could also cause stronger negative individualistic behaviour.

Hill (1990) claimed that there are individuals who will give priority to cooperation and trust and will not initiate opportunistic behaviour and analysing only agency framework may lead to neglecting ethical aspects, cultural aspects, ignoring the development of distrust for and disrespect of the agent.

The Islamic organisations have been studied in the context of the principal-agent relationship (Haque & Mirakhor, 1986; Bashir, 1996). However, there is an additional cost of agency in Islamic companies when all transactions need to be *Shariah* compliant

(Safieddine, 2009). Investors in an Islamic company can invest based on three financing modes: partnership, trade and rent, which all are based on the principle of profit and loss sharing between banks and investors. This practice adds an additional agency problem due to separation of cash from the control (Siddiqui, 2001; Siddiqi, 2006). In such cases, managers would not identify best opportunities on behalf of a customer through negligence or by not making sufficient effort in managing the funds of investors in a *Shariah* compliant manner, which might result in lower profit and increase their benefits (Dar & Presley, 2000; Grais & Pellegrini, 2006). In the same vein, Bashir (1999) stated that, an Islamic bank can play two roles, the role of owner when it lends money to its customers on the profit and loss sharing basis as well as the role of agent when it accepts deposits from its customers. However, the customers of Islamic banks get exposed to greater risk, as they are not entitled to receive fixed returns on their deposit and there is no guarantee that value of the deposit will be preserved. They might end up getting less than what they deposited. Given the conventional financial institutions aim to maximise shareholders' value or profit, what would be the influence of Islamic financial instruments when considering or implementing the cross-border M&A? This question will be explored by analysing the response of interviewees in organisations under study.

An extensive control may be required to evaluate management performance in Islamic companies. This may encourage a change in agency behaviour and it may help to mitigate the issue of managers trying to satisfy their own interest (Shapiro, 2005). However, some scholars such as Dharwadkar et al. (2000), Abu-Tapanjeh (2009) and Shamsuddin & Ismail (2013) have pointed out that the strength of shared religious beliefs can support a culture that can counter some of the self-serving agency behaviour. Notwithstanding this, the role of financial rewards for *Shariah* scholars needs to be carefully examined.

Management in Islamic companies experience different kind of work in terms of: dealing with different financial instruments; different obligations to the depositors and different types of capital financing. Thus, they experience different relationships with the concerned parties in order to comply with *Shariah* (Aggarwal & Yousef, 2000;

Chapra & Ahmed, 2002). This extends the agency problem beyond the normal separation of ownership and control. In Islamic companies, SSB strongly influences the outcome of any strategic decision-making; therefore, additional layers of internal and external *Shariah* auditing are required to mitigate possible opportunistic behaviour and to reduce information asymmetry in financial reporting (Abdul Rahman & Haneem, 2006).

Managers in Islamic companies should be accountable not only to the company, its shareholders and all stakeholders, but also to the Almighty *Allah* with the aim of creating better welfare and development to the society (Siddiqui, 2008; Abu-Tapanjeh, 2009). Islamic perspective with the special notion of *Tawhid* (Unity of *Allah*) educates company's members to put into practice aspects of *Ikhlas* (sincerity), *Itqan* (wellinformed), *Amanah* (truthfulness) and *Shura* (consultation), not only in the financial reward/outcome but also in religious rewards (Chapra & Ahmed, 2002; Iqbal & Lewis, 2009). However, the moral relativism argues that the entire ethical values are mainly derived from Government regulations or communal surroundings and there might be no complete decency or complete evil in a relativist culture (Rice, 1999; RagabRizk, 2008).

Agency theory has been criticized by Donaldson & Davis (1990) on the grounds of its methodology, individualism, narrow-definition, disregard for other research, organizational economics, CG defensiveness and ideological framework, such that it focuses only on individual rather than organisational behaviour. Noreen (1988) also criticised agency theory because it focusses on opportunistic behaviour of the minority and not the majority. So, to what extent the agency theory relevant in the context of the Islamic CG where it displays an additional layer compared to the conventional CG? Does it have any explanatory powers of the behaviours and actions of BOD, SSB and *Shariah* scholars? Do these agents possess relevant business knowledge, expertise, and behaviour which promote the interest of the business owners such as shareholders and customers as the latter were also found to be the main source of funding for the Islamic financial institutions in the study context?.

There is also a structural problem commonly found in Islamic companies as they tend to be family owned companies. The ownership structure is one of the agency theory concerns and has influence on the CG practices as it can increase the cost when firms have complicated highly concentrated ownership structure (Gogineni et al., 2010). Kapopoulos & Lazaretou (2007) observed that when family members exist in the top management, there is an additional layer of agency behaviour and the opportunity for free and objective consultation which can otherwise exist in a BOD is lost.

### **2.15.3 Stakeholders' Theory**

The concept of stakeholders has been embedded in management discipline and managers' thinking since 1970 (Donaldson & Preston, 1995). Several scholars such as Freeman (1984); Harrison & John (1994); Clarkson (1995) and Rowley & Berman (2000) have developed and reviewed stakeholders' theory. Stakeholders' theory has pushed the boundaries beyond the vision of profit maximization to include the welfare of all stakeholders (Mitchell et al., 1997). This theory attempts to understand the relationship that exists between corporations and its stakeholders. It also tries to address a fundamental question: which group of stakeholders deserves and requires management's attention (Abdullah & Valentine, 2009).

Freeman (1984) initially suggested that the firm is accountable for creating wealth for owners. Later, the author developed the theory to address the interest of a wider range of stakeholders and for protecting the interest of other non-financial stakeholders. The theory takes into cognisance the relationship between an organisation, people and other organisations in the environment and this affects the decision- making process and the outcomes of the firm. Clarkson (1995) proposed that the purpose of the firm is to build stakeholders' wealth. Berman (1999) provided empirical evidence that good stakeholders' management has a positive impact on corporate performance and reputation.



Stakeholders have been defined by Freedman (1984: 46) as “any group or individual who can affect or is affected by the achievement of the organization’s objectives”. Moreover, Alkhafaji (1989: 36) defined stakeholders as “groups to whom the corporation is responsible”. Greenwood (2007) defined stakeholders as those who are located in the community and have power to affect corporate activities or can be affected by corporate operations. In contrast, there are some scholars who take a narrower view of stakeholders such as Clarkson (1994: 5) who stated that “voluntary stakeholders bear some form of risk as a result of having invested some form of capital, human or financial, something of value, in a firm”.

Based on those definitions, stakeholder identification includes external and internal stakeholders. Internal stakeholders are employees, managers and owners, while external stakeholders are customers, shareholders, suppliers, creditors, Government and the society (de Chernatony & Harris, 2000). All stakeholders have a network within the organisation to serve the business goals (Freeman, 1999). Post et al (2002) asserted that the traditional role of organization is to create wealth for all stakeholders. Maak (2007) and Du et al. (2010) have agreed with the idea of broader set of stakeholders, all being important and no group of interests can be dominated by others.

However, Wheeler et al. (2002) argued that stakeholder’s theory incorporates the sociological and organizational disciplines. In that landmark, stakeholders’ theory is more of a broad theory derived from a combination of many subjects such as philosophy, ethics, politics, economics and law (Abdullah & Valentine, 2009).

Some scholars such as Andriof et al. (2002); Burchell & Cook (2006) and Cooper & Owen (2007) have extensively reviewed and supported this theory in order to explain organisational behaviour towards its stakeholders. However, there are also other scholars such as Sundaram & Inkpen (2004), who argued that stakeholders require management’s attention. Whereas, Donaldson & Preston (1995) assumed that all groups of stakeholders are involved in the business activities to obtain benefits. Stieb (2009)

criticised this theory and argued that Freeman's (1984) propositions focuses on the protection of interests of all stakeholders and aimed at a careless transfer of decision-making power and wealth.

The propositions of the stakeholder theory can be divided into three main approaches which are descriptive, normative and instrumental (Freeman, 1999; Jawahar & McLaughlin, 2001; Hendry, 2001). The descriptive approach plays more informative role as it is concerned about the real corporate actions with respect to its stakeholder and it reports what is actually happening in the organisation. Donaldson & Preston (1995) argued that the descriptive aspect can be used as a guide by managers in order to achieve corporations' operations in a way that all stakeholders benefit from the entity. The normative approach is supported by Freeman (1994) and it is the central and foundational of stakeholders' theory and goes a long way in determining the ideas of different groups of stakeholders, corporate activities and interest of all stakeholders. This approach, considers ethical issues of an entity that should be considered and what is morally right or wrong. The development of the other two aspects relies on the decisions involved in the normative stage (Introna & Pouloudi, 1999). The instrumental approach is more predictive and practical as it integrates and evaluates other aspects. It attempts to assess management decisions and tries to link the reality with the outcomes. In addition, it suggests that in order to avoid or accomplish a specific response from the stakeholders, community involvement activities are required (Pesqueux & DamakAyadi, 2005). In this study context, the researcher believes that both the normative and instrumental dimensions of the stakeholder theory to have potential to explain the behaviour of agents such as managers, BOD, SSB, *Shariah* scholars and hence to be used in this study.

Neville & Menguc (2006) argued that stakeholders' reaction is affected by management decisions of specific organisation behaviour which can be viewed as either instrumentally or normatively motivated. Jones (1995) noted that stakeholders' theory is helpful for predictions of stakeholders' actions as well as reactions. In addition, Mitchell et al. (1997) suggested that this theory is concerned with which groups of stakeholders deserves or require managerial attention.

In terms of cross-border M&A deals, organisations may be exposed to different stakeholders' responses. Hitt et al. (2001) explored the key issue of M&A that impact all stakeholders. They argued that the reaction of stakeholders is often negative as there have been several poorly performed cross-border M&A, mainly due to the complexity of the process and the challenges involved. Wood & Jones (1995) argued that evaluation and expectations of stakeholders' reactions would provide a better understanding of all stakeholders, thus, reduce the gap between stakeholders and management through better disclosure. Employing the stakeholder theory in this study provides useful information in order to explain the impact of wider groups of Islamic organisations' stakeholders on such business deals based on their values and beliefs.

Despite the popularity of Stakeholders' theory in many fields such as business and law, it has been criticised as not being a coherent theory having been developed by a number of different scholars, beginning with Freeman (1984). Another issue is that although Freeman identified both internal and external stakeholders, the almost limitless linkages between these groups and between the individuals have not been fully mapped out and therefore the theory lacks a real conceptual basis for explaining a firm (Key, 1999). Similarly, Donaldson & Preston (1995) argued that stakeholders should be identified by their interests but they emphasised the difficulty in defining them and what actually constitutes their interest. Agle et al. (2008) argued that the theory faces some challenges. One of the challenges is that the theory is unable to provide a distinct standard to measure managers' performances and environmental assessment (Sacconi, 2006). Sternberg (1997) criticised the idea of directors and managers having to accept everybody as stakeholders. Mitchell et al. (1997) argued that it is not fully developed and more work is needed.

In its current form, the conventional stakeholder theory may lack explanatory power to explain what is happening in the study context. This is because the Islamic perspective of the stakeholder goes beyond the conventional perspective. It arises not only in the

business practices but also above all, the values which guide Islamic organisations to be expressed in the transactions and social roles (Dusuki, 2008). The objective of *Shariah* is to promote social and economic objectives, however, some scholars such as El-Gamal (2006); Dusuki & Dar (2007) and Azid, et al. (2007) claim that no fundamental differences between Islamic and conventional organisations as social roles of Islamic practices are similar to the social welfare goals of the conventional practices.

Azhar & Afandi (2003) argued that previous literature focuses on economic aspects of the Islamic firms whereas social values of Islamic perspective are excluded to the backseat in the discussion. Essentially, many Islamic economists including Chapra (1985), Ghosh et al. (1996), Haase, (2014), Farooq & Zaheer (2015) and Siddiqui (2001) emphasised that the Islamic philosophy of business offers a more stable and balanced as well as solid society as it prohibits interest, gambling and excessive risk to protect all stakeholders. Islamic objective of any business entity is to seek balance between earnings and spending in order to achieve a socio-economic benefit for all parties in the society (Haron & Hisham, 2003; Dusuki & Bouheraoua; 2011).

In the light of conventional perspective, the aim of the management is to maximize the profit of shareholders and their financial interest while other stakeholders should safeguard themselves by the law (Blair & Stout, 2001). However, the Islamic system of businesses are based on a principle of no-injury “*Maslahah*”, therefore, they are not supposed to maximize profit for shareholders at the expense of social responsibility and commitments to brotherhood and justice (Bashir, 2001). Furthermore, based on Islamic property right and contractual agreement, the right of an individual is guaranteed as long as such right is not in disagreement with the interest and wellbeing of the society (Iqbal & Mirakhor, 2004; Obid & Naysary, 2014).

The discussion in the above two paragraphs showed how some CG values and principles could be perceived and interpreted in different lenses due to cultural and religious influence. Whilst businesses in the Western context exist to maximise the shareholder values and to make profit, the intake from the *Shariah*- based CG is different as it advocates fairness, well-being, and social responsibility for the community and society in general. Therefore, the context in which these three countries

firms found themselves could provide rich insights into the strengths and limitations of the taken granted views of the stakeholder theory's explanatory power when considering the cross-border M&A between the Islamic financial companies in the three Gulf countries and non-Islamic countries from the West.

## **2.16 Chapter Summary**

This chapter reviewed relevant contextual and empirical literatures, and theories. The literature review covered and compared both Islamic and conventional CG, various CG models adopted in different parts of the world, CG mechanisms, and the corporate legal structures of the three countries under study. Then it went on reviewing the underlying philosophical assumptions and the spirit and letter of *Shariah* principles followed by the Islamic CG model, *shariah* compliance, Islamic financial instruments and three theories underpinning the CG. In the process, the literature review identified the merits and limitations of the reviewed concepts, approaches, and issues and identified gaps for this study. As a summary, the literature review found:

- Similarities and difference between the Islamic and conventional CG.
- The emergent nature of the Islamic CG and how it is grounded in *Shariah* law and principles, and how such grounding influence the Islamic financial companies' motivation and behaviour when seeking to engage in the cross-border M&A.
- The distinctiveness of the Islamic corporate mechanisms (ownership structure, composition and selection of BOD, SSB, *Shariah*-based disclosure and transparency) and its potential on enabling or constraining the cross-border M&A.
- The likely influences of the subjective interpretations of the *Shariah* Scholars on managing practices of Islamic financial companies
- The development of Islamic finance and, in particular, the Islamic financial instruments and whether these could positively or negatively impact on the potential cross-border M&A.
- The limitations of the taken granted view of the stewardship, agency and stakeholder theories in understanding the behaviour of various agents in the

context of Gulf countries and how the study context would help to extend and enrich these theories.

As far as this researcher's knowledge, no previous research studied the influence of *Shariah* principle on cross-border M&A between Islamic financial companies and non-Islamic companies. Previous studies, for example, focused on Board effectiveness in the level of disclosure and transparency of Gulf corporations (BDI, 2013), cultural and Islamic beliefs on CG practices (Bakhtari, 1995; Saidi, 2004; Haniffa & Cooke, 2005; Hidayah, 2014), to what extent Anglo-Saxon and combination models of CG principles applied in the Gulf region (Lim et al. 2007). In their studies of governance practices, Baydoun et al. (2012) also found that there is rarely any separation between ownership and management, as friends and relatives dominate the BOD. Haque & Mirakhor (1986) Bashir (1996) studied the principal-agent relationship in the Islamic organisations. The literature review thus showed that no previous studies examined the influence of *Shariah* CG principles on the cross-border M&A in a holistic manner. The researcher believes that this study is the first of its kind to examine this issue rigorously taking the case of three Gulf countries, multiple case study organisations, and tapping into the understanding, interpretations, of various stakeholders.

However, a common method of growing the business by expanding into different markets and benefit from globalisation is through cross-border M&A. The move towards *Shariah* compliance in such a case creates a fundamentally divergent financing situation due to prohibition of interest or *Riba* in and also limits the sectors of growth due to prohibited activities such as gambling, alcohol and certain types of entertainment etc. Therefore, not surprisingly the literature has reported low success in M&A between Islamic and non-Islamic companies. In terms of theoretical underpinning, this chapter contains an overview of three theories which are the dominant theories of CG, including agency theory, stakeholder theory and stewardship theory. Each of these theories are briefly explained along with their critique and discussed in the context of both the conventional and *Shariah* CG. The next chapter explains the research design, methodology adopted and justification for adoption.

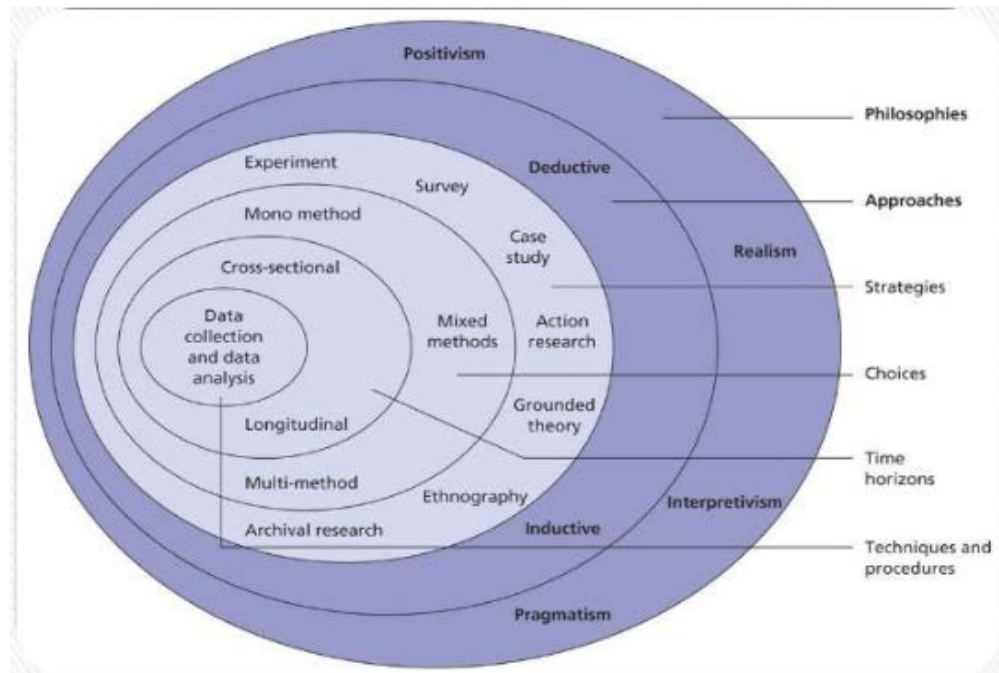
## **CHAPTER THREE: RESEARCH METHODOLOGY**

### **3.1 Introduction**

The last two chapters provided sufficient background to choose an appropriate research methodology in order to deal with the research aims and questions. The chapter is organised into several sections. The first four subsections deal with general issues relating to philosophical and epistemological assumptions and the research approaches. This is followed, in several sub-sections, by research methodology to provide discussion and then rationales and justification for the chosen research strategy, sampling and sample selection, data collection methods, data analysis and consideration of the research ethics along with a brief summary sub-section.

In order to properly address all the appropriate methodological aspects of this study, the research onion (Figure 3.1 below) introduced by Saunders et al. (2009) will be used as a guide, as it provides a well-defined guide for the complete research process. The researcher should peel away several layers of the research onion in order to complete the research process. This chapter focuses on the six layers of the onion, and the discussion starts from the research philosophy to the techniques applied for data collection and analysis.

**Figure 3.1: Research Onion**



Source: Saunders et al. (2009)

### **3.2 Assumption about Social Research**

This research looks at an important aspect of socialisation or the ways of life in a particular setting; hence, it is a social research on one hand. Social research is most often conducted by social scientists to reflect the current situation of modern life and examines a society's attitudes and beliefs toward the changes within it, thus, questions are asked to provide insights on how to approach such issues (Ragin & Amoroso, 2010; Firebaugh, 2008; Bryman, 2012). Social research topics include conceptual and theoretical areas such as politics, criminology, economics and the study of business (Becker et al., 2012). In order to explore and analyse human life, social research finds out the relationship between variables, though it is difficult to understand and predict human behaviour because people are not alike in feelings or emotions (Babbie, 2015). This can be attributed to various factors that might have an effect on the behaviour of human beings such as biological, psychological, socio-cultural and environmental factors (Kangai, 2012).



The influence of *Shariah* principles of CG on cross-border M&A is an aspect of social research. *Shariah* principles of CG were shaped by the influence of Holy Scriptures in *Qur'an* and *Sunnah* teachings (Hameed et al., 2006; Alsanosi, 2009). The *Shariah* law embodies the way of life, and some countries follow the law obediently (Suleiman, 2000). These laws are not limited to spirituality, but also have a great impact on the economy, political, and medical systems (Rice, 1999). Social practices were developed after interpretation of these laws, and quality of life was found to be maintained among Islamic countries (Ibrahim et al., 2011). *Shariah* scholars, in accordance with the Islamic scriptures, and traditions, laid the economic principles of companies working under the Islamic umbrella. The research of this subject further underlines the fact that there are many aspects to consider in designing these robust Islamic economies. The mind-set of the financial institutions and business people in the Gulf countries are quite different from the developed countries (Davis et al., 2000). The strings that pull the CG structure of the Islamic financial companies in the Gulf region rely on the *Qur'an* and *Sunnah* for having a standardized and accepted way of doing business; these sometimes contrast with the Western systems (Abu-Tapanjeh, 2009; Hasan, 2009; Aribi & Gao, 2010). The social values in these countries typically vary from their counterparts in the West, and such differences stand in between them in forming strategic partnerships or M&A (Farook et al., 2011; Baydoun et al., 2012). This subject of social research aspect of understanding the human behaviour of the population inclined towards an economic system that not only integrates their religious beliefs, but also acts as a moral pillar to lean against, was really an interesting topic for further research.

The theory in social research is instrumental in the development of methodology for research purposes. Ragin & Amoroso (2010, p.8) defined social research as “one among many ways of constructing representation of social life - of telling about society, it is the product of the efforts of an individual or group of individuals that addresses socially significant phenomena”. Ragin, (1994) argued that researchers use evidence to test ideas with help of the interaction between ideas and evidence to make sense. Therefore, Social research is mainly concerned about social and cultural dimensions based on logic and observation to reach a valid conclusion.

According to Kangai (2012), there are three reasons that motivate social scientists to devote their lives to develop new knowledge; which includes the desire to improve people's lives and sustain economic growth. There is a lot of emphasis on how human behaviour is melded with new information and development of culture over the years (Bandura, 2002; Rogoff, 2003). In the last three decades, the principles of Islamic finance have been emerged as a form of Islamic legal system and have been practiced by Gulf countries (Babai, 1997). Rice (1999) found that Muslims grew with the foundations of the Islamic economic ideals, and they are ingrained since their inception. However, the behavioural change happened through intrinsic exposure to the new ways of doing business. Muslims should share their business ethics to help managers of the West countries to understand Muslims' perspectives, which is an aspect that this study is interested in exploring.

However, considering that social scientists such as Blanche et al. (2006); Berg et al., (2004) and Bryman (2015) conduct social research by following a systematic plan, including the choice between quantitative and qualitative methods used for this kind of research, these are explained in detail in subsequent sections. The relationship between social research and theory can be noted at early stage of research when the research problem and question are identified (Bernard & Bernard, 2012).

This study is intended to investigate how *Shariah* principles influence cross-border M&A between Islamic financial companies (banks and insurance) in Gulf countries namely; Saudi Arabia, Kuwait and UAE and non-Islamic companies in the Western countries, in effect; the research question is looking at how the complex conventional issues relating to various leadership styles; managing organisational and people's cultural differences as well as managing financial and legal risk, to which are added the *Shariah* related issues can affect the formulation of cross-border M&A with non-Islamic countries.

### **3.3 Philosophical Assumptions**

Research means different things to different people; therefore, they bring their personal worldviews and perspectives to whatever study they are undertaking by moving towards their subject via explicit or implicit assumptions that end up shaping the direction of their research (Burrell & Morgan, 1979; Collis & Hussey 2009). Burrell & Morgan (1979) suggested that such perceptions underpinning different approaches to research are influenced by epistemology, ontology and axiology. Although philosophical ideas are hidden, these perceptions influence the different stages of conducting a research, from data collection to the actual findings of a study (Slife & Williams, 1995; Ryan et al., 2002; Creswell, 2013). The practice of research involves philosophical assumptions, ideas combined with strategies and implemented with specific methods. However, it is noteworthy to point that the intention here is not to decide the best philosophical reasoning that suits social research, rather to clarify the philosophical stance of this study (Sutrisna, 2009).

There is a general agreement on research framework being a combination of three elements. These elements are; philosophical assumptions, general procedure “strategies” and detailed procedure “data collections” (Creswell et al., 2003; Collis & Hussey, 2009). The discussion of the above should be followed by the justifications for choosing an approach over another in designing research.

Researchers including Sayer (1984); Creswell (2009) and Jonker & Pennink (2010) believed that in undertaking research, investigators also bring their own perspectives of the world to their research. The philosophy adopted by researchers contains important presuppositions about the way in which researchers view the world (Johnson & Onwuegbuzie, 2004).

These presuppositions will underpin the research and work as under-labourer and drive the research strategy and the methods (Bryman, 2011; Bryman & Bell, 2015). In contrast, the research philosophy that is adopted by a researcher will be influenced by

how the researcher's view (Bryman, 2012). In this section, three different ways of thoughts about research philosophy will be discussed namely: epistemology, ontology, methodology and methods, and they all will influence the research process.

These assumptions guide the research process from collecting data to interpretation of the results (Ryan et al., 2002; Creswell, 2009). It is argued that the central idea of social research is how the researcher understands and interprets data to address whether social entities exist separate from social actors (Johnson & Turner, 2003; Bailey, 2008). In addition, a researcher reflects the research position by the conduct and reporting of their work based on the philosophical assumption (Walsham, 1995). Subsequently, the development of methodology by researchers is influenced by the different epistemologies, ontologies and human nature (Burrell & Morgan, 1979).

### **3.3.1 Epistemology**

Epistemology is the acceptable knowledge and justified of beliefs (Hofer&Pintrich, 1997; Gray, 2009). Epistemology means knowledge and how we create knowledge in an intelligible way (Tellis, 1997; Silverman, 2010). Baptiste (2001) stated that epistemology is the process of knowledge and knowing. Likewise, Cope (2002, p34) stated that "Epistemology is a theory of knowledge with specific reference to the limits and validity of knowledge". It deals with the question of what is the truth, what is the criterion of justified or acceptable knowledge and how individuals understand the world around them. There are different ways to create knowledge: positivist, interpretative, post-positivism and pragmatism epistemology (Creswell, 1998; Ryan et al., 2002; Creswell, 2003).

From the perspective of positivism, the researchers need to act as objectivist; which means they should avoid the involvement of any personal bias influencing the outcome of the research. This approach is only valid for the controlled experiments or quantification of a certain phenomenon. This is very rarely used in the qualitative research (Jones, 2002; Roots, 2007; Creswell, 2009).

Similarly, the epistemology of the interpretative approach involves the method of focusing on the participant/researcher dialogue to uncover the subjugated knowledge and link it to the social behaviours, thereby creating the knowledge through standpoints of the researcher who mediates reflectively about the given research problem (Agger, 2007; Carter & Little, 2007). Likewise, post-positivism epistemology is the changed version of the objectivist in which the researcher believes that existence of pure objectivity is not possible within the real world; and the outcomes of the research may be true or 'probably true' (Creswell, 2009). In contrast to foregoing epistemologies, the pragmatism epistemology takes the pluralistic approach to reconcile the different viewpoints/works with what is known to the researcher (Guba & Lincoln, 1994; Sprague & Kobrynowicz, 2006).

From the above discussion of epistemology, it is obvious that epistemology of each paradigm varies from each other. Furthermore, it can be said that the positivist, interpretivists, post-positivist and pragmatist paradigms have been enormously influential in the development of quantitative and qualitative approaches to social research.

### ***3.3.1.1 Positivism***

In the view of positivism, the researcher builds knowledge on an acceptable theory and rationale foundation as the way to get at truth (Schrag, 1992; Baker, 2000; Johnson & Onwuegbuzie, 2004). In addition, researchers conduct research to test hypotheses using empirical approaches and objectively analyse data by using structured research methods, therefore, a neutral process is followed to discover the truth and this will lead to development of a theory which may be used to do further research (Bryman, 2001). However, based on the findings of any research, positivists may argue that the theory is not valid and there is need to revise it for better prediction of the reality. Positivist believes that experiment is the key method for scientific research and the measurement is essential method that helps to identify features of natural laws (Stahl, 2007). In

general, the social researcher disagrees with this form of research. Positivist is more likely to use well-structured methods in order to enable reproduction (Amaratunga et al., 2002). Knowledge generated by positivist is confirmed by using measurable observation method that offers them with statistical analysis (Merriam, 1991; Guba & Lincoln, 1994; Giddings & Grant, 2007).

### ***3.3.1.2 Realism or post-positivism***

Some scholars such as Comte, Durkheim and Locke came up in the 19<sup>th</sup> century with the realism or post-positivism as a scientific method (Smith, 1983). It is another epistemological position and it refers to the thinking after positivism (Phillips & Burbules, 2000). Post-positivism observes that the way of thinking of different scientists is not distinctly different (Devitt, 1984). It reflects a deterministic philosophy where every action causes a reaction, and every reaction, in turn, becomes the cause of subsequent reactions (Creswell et al., 2003). The knowledge that develops through realism is related directly to the theory of truth which asserts that there is an objective reality that is possible to know based on observation and measurement (House, 1991). Therefore, scientists follow specific methods and measures to guide in the process of uncovering truth about the social world and assure that observations are valid (Miles & Huberman, 1994; Phillips & Burbules, 2000).

### ***3.3.1.3 Interpretative or constructivism***

In addition to the above, another process of knowledge creation that became widely known from Mannheim & Berger in 1967 is interpretativism or constructivism. In this position, the researcher discovers new knowledge from a side existing knowledge (constructivism) (Karaffa, 2015). Based on this approach, knowledge can be obtained by studying the social phenomena in different ways, by undertaking an interpretive approach to discovering the problems (Ayer, 1966; Bransford et al., 1972; Dessler, 1999).

The collation of facts that create basis for laws leads to the generation of knowledge, as Morgan (2007, p.52) suggests that “positivism and constructivism influence how research questions are asked and answered”. As a result, positivism and constructivism perceive epistemological issues in different ways. Constructionists stated that truth does not exist, knowledge is achieved by construction in other words, and the existence of truth or meaning varies with facts or realities in our changing world (Speed, 1991). Meanings are not discovered, but constructed over a period of time, which is needed in order to improve the understanding of issues (Teddlie & Tashakkori, 2003). The construction of meanings also needs to be considered in order to ensure that the truth can be discovered and understood within the wider perspective and this has to be taken into account by the researcher (Giddings & Grant, 2007, Henneberg et al., 2010).

#### ***3.3.1.4 Pragmatism***

Another philosophy about knowledge creation is pragmatism. It came from the work of some writers such as Peirce and James (Cherryholmes, 1992). Here, the choice of one philosophical position or the other is impracticable as researchers in this kind of research may need to use different approaches to better understand the problem (Rossman & Wilson, 1985). In this case, method is not important, but rather, the problem is the most important. Research under this philosophy does not clearly identify the research question either as positivist or interpretivist; therefore, it works with both positions. Subsequently, both “qualitative and quantitative” are highly appropriate for such studies in social research (Tashakkori & Teddlie, 1998).

#### **3.3.2 Ontology**

Ontology is the philosophical study of the nature of being real and related to how the researcher views reality. It is concerned with whether reality exists by itself or individual produces it (Burrell & Morgan, 1979; Sayer, 2000; Ryan et al., 2002; Bahari,

2012). In addition, ontology deals with the question of what is real. Further, it refers to particular rules of behaviour about the nature of humans and their experiences (Patterson & Williams, 1998). Bryman (2001) made a distinction between two main ontological positions, objectivism and constructionism.

Objectivism is closely linked to positivism and the natural sciences, as it describes logical relationships between variables and asserts that a social phenomenon can be seen as a tangible object and independent of social actors (Maxwell, 1992; Bernstein, 2011). On the other hand, constructionism is closely linked to interpretative approach that seeks to understand the meanings of people attach to social realities. It believes that social actors have an active role in constructing social phenomena (Bryman, 2001; Bryman, 2008).

However, Silverman (2001) argued that in practice, such a clear difference between these two ontological positions rarely exists and some researchers combine elements of both approaches.

### **3.4 Philosophical Assumptions Underpinning this Study**

The above mentioned epistemological and ontological assumptions have direct implications for the methodology adopted in this research (Burrell & Morgan, 1979; Hopper & Powell, 1985; Laughlin, 1995; Collis & Hussey, 2009). As well as the outlined primary purpose of this study as mentioned in Chapter One, the researcher is interested in studying the impact of such, rather than trying to change the current situation, as this study is to investigate the influence of *Shariah* CG principles on cross-border M&A between Islamic financial companies in Gulf countries (Saudi Arabia, Kuwait and UAE), and non-Islamic companies in Western countries. Studying organisational and human behaviour, culture, history and situations in which people live and interact can be examined in different contexts through a multiplicity of methods.



Therefore, there are varied and multiple truths that can be found and may not be aligned with the positivist and post-positivist approaches.

Considering this, the research will be hinged on the interpretivist perspective as the researcher would provide some insights that could have policy implications for changing the current practice of Islamic CG as adopted by Islamic organisations. As this research adopts the interpretative perspective, it aligns with the ontological position of constructionism, especially knowing that humans can have an impact on the social world. This would help to find out whether Islamic principles that are implemented within Islamic organisations have an impact on cross-border M&A between Islamic and non-Islamic companies.

### **3.5 Research Methodology**

In the social sciences, there is an ongoing debate among scholars on how research should be conducted (Bulmer, 1979; Marshall & Rossman, 1989; Silverman, 2006, Bryman, 2008). Also, researchers are believed to introduce their own perspectives to their research (Jonker & Pennink, 2010), which then makes a clear statement of the chosen methodology or methods. The research methodology provides a clear overview about the methods used for gathering data and techniques used to analyse data which are the focus of the methodological assumptions.

#### **3.5.1 Research Approaches and Techniques**

##### ***3.5.1.1 Deductive and Inductive Reasoning***

In this section, two approaches of reasoning and their implications will be explained. Punch, (2013) stated that there are two ways of developing research questions:

deductive approach, which means that the researcher starts by moving from general ideas on the selected topic to develop particular research questions. On the other hand, working inductively starts with a specific question and move from these back to develop more general questions on the topic. Both approaches can be used in listing the research questions, based on the scope of conducting the research (Hyde, 2000; Goel & Dolan, 2004; Elo & Kyngäs, 2008).

The deductive or “top down” approach involves developing a hypothesis based on an existing theory and then the hypothesis is subjected to empirical study (Ali & Birley, 1999). Furthermore, this approach follows conclusion logically as the researcher starts with particular to general questions (Pelissier et al., 2009; Babbie, 2010). In other words, it is started with thinking up a theory then finding new hypotheses to be able to test them by confronting it with observations and finally reaching a conclusion (Snieder & Larner, 2009).

This approach has been discussed by many authors such as Punch (2005, p.38) who contended that ‘we should only have hypotheses when it is appropriate to do so’ and that is only ‘when we have an explanation [a theory] in mind behind our hypotheses’.

This means that the researcher undertakes a good literature review on the selected topic, then based on thorough understanding of the subject, proceeds to build hypotheses. Based on such, the hypothesis will be tested based on the empirical observation of data collected from the primary research and the results analysed accordingly. The deductive approach is used in quantitative research, in which hypothesized relationships are developed and tested. When using a deductive approach, an understanding of the facts being established as well as a detached and objective view of the phenomenon is needed (Carr, 1994).

On the contrary, inductive approach generates the theory as the outcome of the research. This approach is often termed as “Bottom-top”, where the research starts with specific applications or findings, which are then used to move and to draw a broader or general

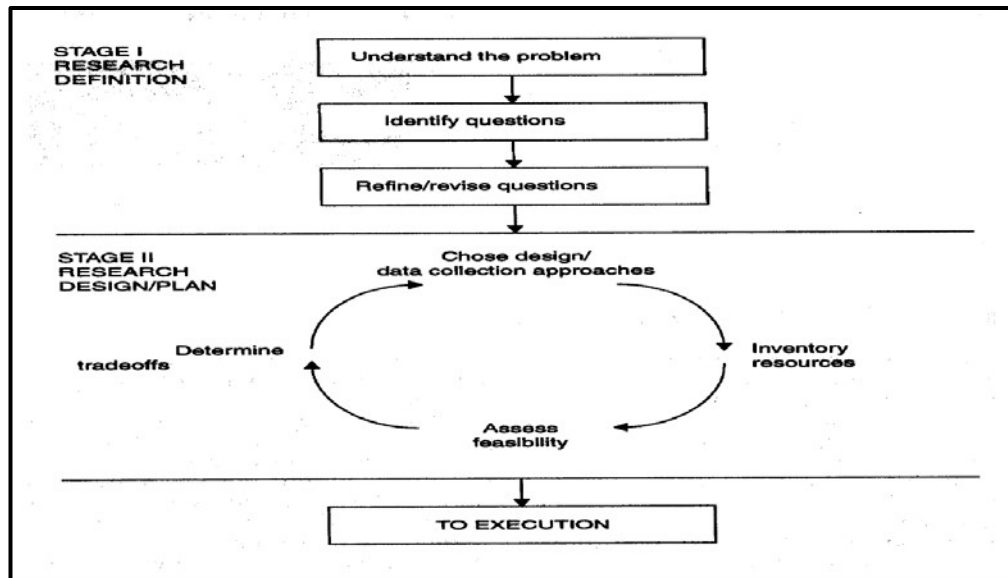
idea of the phenomenon under investigation (Goddard & Melville, 2004). The research starts with narrow focus, and moves to generalise the finding to a broad segment or subject (Porter & Miikkulainen, 2003; Lodico et al, 2010; Bernard, 2011). In this approach, no theories and hypotheses would be applied at the initial stage of the research process, thus findings will be obtained when the study is completed (Lancaster, 2005).

The inductive research adopts methods such as surveys, interviews, focus and group studies to collect research data (Yin, 2015). A researcher will further analyse the data to reach common insights on the subject accordingly. Based on the insights, the researcher will develop a universal theory based on the findings from the sample population accordingly. The next step would be comparing and analysing the newly grounded theory with the existing practices and frameworks. If the new theory forces drastic change in the existing protocols, the researcher has heralded a paradigm shift (Hsieh & Shannon, 2005).

#### ***3.5.1.2 Qualitative and Quantitative Techniques***

When considering a suitable research technique for a specific study, researchers usually consider the choice between qualitative and quantitative techniques, and even the use of both, when applicable (Maxwell et al., 1998; Thomas, 2003). The selecting a suitable research technique to be employed in a study is important to identify the meaning of the collected data (Tashakkori & Teddlie, 1998; Myers, 2013). It is therefore important to differentiate qualitative and quantitative research techniques from each other before discussing which is best suitable for this research. Researchers such as Maxwell et al. (1998) and Bickman et al. (1998) suggested the process of qualitative research design (see figure 4.2).

**Figure 3.2: Research Design**



Source: Bickman et al. (1998)

Qualitative research methods are interpretative and aim to reveal a target audience's range of behaviour and perceptions. Furthermore, De Vaus (2002) noted that these methods provide in-depth data about people's life and help to make sense of their behaviour. It was developed when it was recognised that quantitative methods were unable to deal with human feelings. It uses in-depth investigation of small groups of people and it is based on their words, perceptions, feelings and others, rather than numbers. However, it has been criticized by some authors such as Mishler (1990); Denzin & Lincoln (1994) and Lincoln (1995) as lacking 'scientific' rigour and credibility. In addition, it has been criticised as it is depending on the subjective interpretations of researchers (De Vaus, 2002). Qualitative research is designed to include instruments such as interviews, case studies and focus groups to help in guiding the construction of hypotheses (Bergman, 2008; Creswell, 2012).

Monette et al. (2013) considered that qualitative methods deal with ideas; however, Polonsky & Waller (2005) classified tools such as images, printed word and recorded sound into qualitative methods. The process of qualitative research shows the

relationship between theory and social practices (Bryman et al., 2005), which tends to make it popular in the social sciences as it aids applicability of theory to social issues.

On the other hand, quantitative research methods refer to a type of data that is based on numerical data and dealing with measurement processes. The analysis of the numerical data can be generalised to some larger population (Jick, 1979). It is often a deductive type of research, and the data collection is through surveys, experiments, and longitudinal studies (Teddlie et al., 2008). In social sciences, quantitative research is widely used in fields such as psychology, economics, health and human development. The strength of quantitative research lies in its reliability since it aims to control external variables within a study's internal structure (Carr, 1994). Furthermore, standard testing can assess the data with the use of quantitative technique. This reliability as the strength of quantitative research is a weakness in qualitative research since the latter does not use measurement or quantification to assess data objectively (Gallaire et al., 1984; Teddlie et al., 2008).

However, qualitative research finds strength in validity, whereby fewer threats to external validity are present with regard to this research technique (Kirk & Miller, 1986). This strength could be attributed to the fact that natural setting and controlling factors are fewer compared to conditions in quantitative research, which has to be considered (Tashakkori & Teddlie, 1998). The strength of qualitative research is seen in the characteristic of researchers being immersed in the context and subjective nature of the participants, enabling the researcher to provide an assurance that the data are representative of the subjects (Carr, 1994).

Quantitative method would be preferred when there is a need for objective way to find the solution to the research problem (Punch, 2013). This process often takes short duration of time, and based on the sample size population (Neuman, 2005). This method does not mandate the researcher to be in close proximity with the research

participants unlike the qualitative research methods. The online surveys can help the researcher to collect data from participants from various geographic locations. There are many tools used in quantitative research like the cross tabulation and pie charts to help the researcher to analyse the research data (Patton, 2005). The objective of the quantitative research is usually to test the existing hypotheses, by using appropriate research tools to collect the respective data and further analyse the data to draw inferences which aid confirming, extending and refuting underlying theories (Amaratunga et al., 2002; Sale et al., 2002; Delport, 2005).

### ***3.5.1.3 Relevant Approach and Techniques to the Study***

The choice of the best approach and techniques for this study is challenging as each method has positive and negative features, thus, one cannot be deemed superior to the other. However, scholars such as Creswell & Clark (2007) and Bell & Bryman (2007) have argued that the links between positivism, deductive and quantitative methods on one hand and that between interpretivism, inductive and qualitative techniques on the other are not absolute. Punch (2005) stated that there is no necessary connection between aim of a study and approach as the two strategies can be used for both theory verification and generation.

Since this study focuses on CG across countries with a unique societal attitude due to the practice of *Shariah* law, which has an impact on the development of the Islamic companies and might have effect on foreign transactions, including cross-border M&A, it might be therefore difficult to employ deductive approach as *Shariah* law cannot be objective. This research tends to rely on a high level of qualitative research method to study how the *Shariah* principles such as the prohibition of *Riba*, Islamic inheritance law, limited Islamic financial instruments and the existence of *Shariah* supervisory Board in the Islamic companies might affect cross-border M&A. This could imply the appropriateness of an inductive approach, however, there are chances that data could also be analysed quantitatively, which will strike a balance between deductive and inductive approaches. This is supported by Saunders et al. (2007) view that there exists

a certain overlap in how these two methods are to be deployed based on the scope and objective of the research.

Social scientists often use a mix of these two approaches to identify the best solution to study human behaviours, and how these behaviours are affected by soft religious principles in doing business. This study adopts the inductive approach as it begins with specific findings of cross-border M&A and CG from an Islamic perspective, which serves as basis for drawing a general idea of such phenomenon.

The inapplicability of qualitative technique to this study is evidently seen in its necessity to tackle the research problem in-depth, which requires no element of quantification or measurement. Although, this study cannot rely on a quantitative approach, it is believed that the combination of the two techniques will give this study a good representation (Charmaz, 2001; Saldana, 2015; Davies & Hughes, 2014). There are benefits for using both types of research techniques, and researchers select the appropriate process based on the scope and objectives of the research, and this helps the researcher to understand wider perspective of the participants (Fontana & Frey, 1994; Jankowski & Jensen, 2002; Silverman, 2010).

The researcher used Mono method (qualitative) technique, which was initially developed in the field of social science, with the aim of aiding researchers to tackle social and cultural phenomena, as also identified in the literature (Corti & Bishop, 2005, Curry et al., 2009). Primary data was collected through semi-structure interviews from the sample population and was analysed to investigate the influence of *Shariah* on cross-border M&A in the selected Gulf countries. The available secondary data was used to gather information about Islamic CG including published articles, journals, CG manuals and any statutory publications based on *Shariah* Law.

**Table 3.1: Summary of this Research Paradigm**

Paradigm	<b>Interpretivism (constructivism).</b>
Approach	
Epistemology	Subjective
Ontology	Relativism
Methods	Qualitative

### **3.5.2 Research Strategy**

In addition to the research approach, the type of question that the research project attempts to answer impacts the research strategy (Denscombe, 2010). Research strategy is defined by Saunders et al. (2007) as the development of a plan on how the researcher will achieve the research aim. In the same vein, Lewis (2009) posited that choosing a research strategy provides overall direction to the study under investigation and lead to the decision which is followed by selection of research approach. While choosing a research strategy, three significant factors need to be considered namely, the research questions that need to be answered, the researcher's control over actual behavioural events and the degree to which the research focus on current against past events (Yin, 2013).

Yin (2003b), Creswell et al. (2003), Saunders et al (2009) and Collis & Hussey (2009) argued that while several research strategies exist in business and management including survey, case study, action research, grounded theory, ethnography, cross sectional and longitudinal studies, it is important to select the appropriate strategy for a



particular research study. Case study and grounded theory were adapted as research strategies in this research.

### ***3.5.2.1 Case Study***

Many researchers adopt case study as one of the preferred research strategies (Remenyi, 2002). Fridlund (1997) defined case study as research strategy in which an empirical investigation in details is carried out on a particular subject, which might be a single person or community, family, team or an organization. The author also stated that it is considered to be the most preferred method of undertaking a research when question like 'How' and 'Why' needs to be answered, therefore, in this role it can be used for exploratory, descriptive or explanatory research. Generally, according to Simons (2009) such a method is adopted in circumstances when survey or experimental approaches cannot be adopted or fail to fit in with the requirements of the research. Case study presents many advantages such as obtaining in-depth data with regard to a specific phenomenon by using various methods and offer better understandings that might not be achieved with other strategies. In contrast, there are scepticisms of using case study research such as difficulty in conducting and producing a massive amount of documentation (Baxter & Jack, 2008). However, Fellows & Liu (2008) argued that this can be avoided by organising and managing the data systematically. Another criticism is that it is difficult to reach a general conclusion when using case study strategy due to limited sampling cases (Tellis, 1997).

Bryman (2008) stated that there is a link between the qualitative researches and case study; however, such an association is not absolute as it can be used for both qualitative and quantitative research. Similarly, Dul & Hak (2008) stated that case study should be analysed in a qualitative method. Selection of a research strategy is based on the type of research question (Berg et al., 2004; Saunders et al., 2009). Yin (2013) stated that case study approach is one of the best approaches for presenting evidences in linear format. Further, in such an approach, the researcher is directly involved in collection of data thus making the research ethically justifiable.

### ***3.5.2.2 Rational for adopting case study in this research***

Case study was adopted in this research to develop answers to the research questions that this research intended to investigate (see 1.4 in chapter one). The vast majority of the interview questions were objective about what the (managers, lawyers and *Shariah* scholars) knew about the influence of *Shariah* principles on cross-border M&A between Islamic and non-Islamic financial companies as well as how and why they took certain decisions.

The research questions are mostly consist of how and why type that favouring a case study research. Adopting case study strategy allows the researcher to answer the questions that are investigated in this study, which favoured qualitative method (Yin, 2003b). In-depth knowledge was gained from semi-structured interviews which allow the researcher to address the research aims and answer the research questions reasonably.

Furthermore, choosing case study was due to a number of reasons. The researcher was seeking to compare three Islamic banks and two insurance companies in each of the selected Gulf countries to provide better understanding of Islamic CG and to see whether there are any variations in the implementation of *Shariah* principles. In addition, according to Yin (2003b) another reason to adopt case study as a research strategy is that when the researcher control over actual behavioural events cannot be manipulated. In this research, the researcher was an observer outside the case and did not have control over the behaviour of management of Islamic financial companies. In addition, case study is adopted when studying a contemporary phenomenon as opposed to historical. This study is to improve the current Gulf countries CG practices and cross-border M&A as contemporary phenomenon, and to investigate cultural and religious influences affecting cross-border M&A between Islamic and non-Islamic financial companies. Moreover, based on the philosophical underpinning of this study which was

positioned with an interpretive perspective as well as the nature of the research questions, the researcher decided to use case study as it is often associated with interpretivism (Gerring, 2007).

### **3.5.2.3 Grounded Theory**

Grounded theory is used along with case study in this research to analyse the qualitative data collected through interviews. It is defined as “the theory derived from data, systematically gathered and analysed through the research process” (Strauss & Corbin, 1998, p. 12). The adoption of grounded theory in this study was due to the existence of only limited studies in the subject area and several questions about CG to develop a perception of the influence of *Shariah* CG principles on cross-border M&A in Gulf countries (Saudi Arabia, Kuwait and UAE). This strategy provides a clear direction from collecting data to conclusion (Suddaby, 2006).

Although significant literature related to *Shariah* CG exists, this research is not based on previous literature as no research focuses on the influence of *Shariah* CG principles in the cross-border M&A between Islamic and non-Islamic financial companies. Therefore, this study extends the current literature by identifying barriers to M&A deals between the Islamic and non-Islamic financial companies and provides a critical perspective, while most of the literature tends to be uncritical but promotional. This exceptional situation motivated the researcher to study what are the obstacles to the success of cross-border M&A of these companies.

In order to analyse interview data, Strauss & Corbin (1998) proposed the following steps: the process involves several stages of data collection and modification of information in order to address the questions of when, where, why and how from explanation of phenomena under study. In this case, the researcher seeks a set of concepts thorough a process of grouping as categories and subcategories. This study

identified seven major themes and twenty-three sub-themes from the interviews identified in Chapter Five: Finally, the researcher identified the whole story integrated from the themes and sub-themes and produced the theory about the research problem (Corbin & Strauss, 1990).

#### ***3.5.2.4 Rational for not Choosing other Research Strategies [ may need to tightening]***

There are many reasons due to inapplicability of other strategies such as experiment, survey and ethnography. In this study, the researcher control over the phenomena cannot be manipulated, thus, experiment as compared with case study and grounded theory was considered less applicable to this study as the experiment is to investigate a situation in a laboratory or experimental setting and the experimenter manipulates independent variables to observe its effect on the dependent variables in order to better understand the phenomena (Keppel, 1991; Collis & Hussey, 2009).

Moreover, as compared to a survey as a research strategy, this study used less number of samples than in a survey but with greater details (Saunders et al., 2009; Yin, 2011). In addition, data was collected from limited organisations to explore different issues by comparing them with the intent to generalising, to all other organisations of the same type (Babbie, 1990; Creswell, 2003).

Furthermore, the ethnographic research is usually done due to the ease of doing the research, and proximity of the research participants, which can save the time and resources of the researcher (Spradley, 1979, LeCompte et al., 1993). Ethnographic research can also examine the circumstances which often dictate that the researcher does quantitative research if the research scope is deductive to a specific narrow focus based on the responses from the sample population, and this can help in examining the different issues. Ethnography requires the researcher to be immersed in a setting as a participant observer (Atkinson et al., 2001; Easterby-Smith et al., 2008). As the

researcher was outside to the context in this research, ethnography did not seem to be an appropriate strategy for this research.

### **3.6 Data Collection**

The collection and interpretation of qualitative data must be undertaken in a systematic way (Saunders et al., 2007). This section presents the procedures used to gather data from the prospective interviewee and the way the researcher analysed the data.

The process of data collection is important to explore the issue under investigation and the awareness of individuals of circumstances surrounding and how they shape peoples' experience (Polkinghorne, 2005). As a result, it influences people's behaviour of creating meaning. There are many qualitative methods to collect data, and interview method has been widely used by researchers to gain participants point of view regarding research problem (Kothari, 2004; DiCicco-Bloom & Crabtree, 2006). There are three types of interviews, which are structured, semi-structured and unstructured interviews (Sekaran & Bougie, 2010). These interviews can be administered face-to-face, by telephone or online (Hair et al, 2007).

In the case of structured interviews, all respondents are asked the same questions. List of questions will be pre-planned to help the interviewer to gather a greater depth of information about the research topic under study. However, in order to get sufficient information, high quality questions are required to examine the level of understanding a respondent has about a particular topic (Johnson, Turner, 2003).

In contrast, unstructured interview does not require any predetermined questions and it does not reflect any theories or ideas (Polkinghorne, 2005). This kind of interviews may be used where particular depth is needed. There are many disadvantages of this

technique such as time-consuming, difficulties in managing data and the lack of guidance for the questions (Gill et al., 2008).

Semi-structured interview involves several key questions that help to guide and explore the research issues (Longhurst, 2003). It allows the interviewer to pursue an idea or response in more detail. In comparison with the structured interviews, this approach is more flexible due to the possibility to discover more information by asking prompt questions that not have previously been thought of (Louise & While 1994; Gill et al., 2008).

To fulfil the purpose of the current research, it is essential to use method that allows participants to express themselves and their understanding, views, experiences and motivations freely. In addition, conducting interview could bring unconsidered factors that might affect the research and, thus, provides unexpected insights by a range of different personal opinions, therefore, support to creating-meaning to the research (Gill, 2008).

In this study, the researcher adopted the semi-structured interview and these were conducted face to face as well as over the phone. There are many factors impacted on conducting interviews such as time, accessibility, costs and duration (Hair et al., 2007; Rubin & Rubin, 2011). When this type of interview is conducted face to face, it supports eliciting the in-depth responses from the participants of the study. Furthermore, it also helps respondents to understand the question clearly (Sekaran & Bougie, 2010). The potential limitations of this process involve the 'probable influence' of the researcher on the responses of the interviewees through impressive exchange of words/opinions during conversation, that may lead to development of element of biasness in the derivation of findings from the data (Sturges & Hanrahan, 2004). On the other hand, with the telephone interview there is a freedom to talk freely and it can minimise costs associated with time and finances, especially travelling and maintenance (Holbrook et al., 2003). However, the limitation in the case of telephone interview is that the absence of the body language of respondents (Saunders et al., 2009).

### **3.6.1 Research Population**

The research population of this study comprises all banks and insurance companies in Saudi-Arabia, Kuwait and United Arab Emirate- the three GCC countries under study. The financial sector in the GCC though comparable to that of developed economies, is characterised by the dominance of the banks, monopolistic competition and large presence of domestic players and state-owned banks (Al and Calice, 2016)

-Hassan et

The number of commercial banks operating in the Kingdom reached 25 (23 licenced and fully operational and 2 are licensed but have not yet started operation) at the end of 2015, including branches of foreign banks. Islamic banking asset represent about 50 per cent of all the banking assets in the country as of 2016. Up to the end of 2015, the number of insurance and reinsurance companies that have already been approved by the Council of Ministers reached 35, in addition to 213 insurance service providers to support insurance services.

According to the Central Bank of Kuwait (2015) Financial Stability Report, the banking sector dominates the financial sector of the country accounting for around 82% of the domestic financial sector. Domestic banking sector consists of five conventional, five Islamic and one specialized bank. There are also 12 foreign -owned banks operating in the country of which 5 appear to be conventional, some of them with Islamic windows. The report shows that with 60.7% share as of December 2015, the conventional banking dominates the banking sector followed by Islamic banks, with 38.3% share in consolidated banking system. This makes Kuwait the country with one of the most significant presence of Islamic banks in any country across the globe with a dual banking system. Investment companies are the second major player in the domestic financial system with around 14% share as of December 2015. Investment funds, insurance companies, and exchange companies constitute the rest.

In the UAE, according to the Central bank of UAE, there are 21 domestic and 28 foreign banks operating in the country. Though greater in number, the latter tend to have a very few branches when compared to the national banks. The Islamic banking however account for only 19.6 percent in the market share in 2016 (IFBS, 2017), the rest being accounted by the conventional banking system. The total of 19 banks operate in the UAE of which 11 are Islamic and 8 are conventional banks with Islamic windows. In terms of insurance, the UAE and Saudi Arabia are the Gulf's two major insurance markets, accounting for more than 70.0% of the total premium collected in 2014 (Alpen, 2015). As of 2012, the UAE had the biggest insurance market in the Gulf, with over 60 firms offering conventional and Islamic insurance (Takaful). It is important to remind a reader here the difficulty of getting accurate figures on breakdown of Islamic and non-Islamic insurance companies in Gulf as the numbers of firms changes over time due to some firms being closed and others taken over. Issues such as family ownership of firms and restriction on the entry and ownership share of foreign companies also limits the ways in which insurance firms operate in these countries and is likely to increase a number of Islamic insurance companies as compared to non-Islamic though the latter may have better share in the market.

**Table 3.1 – Population of the study**

	KSA			Kuwait			United Arab Emirates		
	Islamic	conventional	Total	Islamic	Conventional	Total	Islamic	Conventional	Total
Banks	19	6	25	12	11	23	30	21	51
Insurance	26	9	35	11		11			60
			60			34			111



As this study seeks to examine the variations, if any, in awareness, adoption, mechanisms of *Shariah* CG principles, legal structure, and M&A between conventional and Islamic financial companies in the three Gulf countries, the researcher purposively selected 15 financial institutions from the many described above. The key criteria for selecting banks and insurance companies is that they should be operating in M&A context. So, all the chosen 9 banks and 6 insurance companies from the three Gulf countries are those involved in M&A activities. The choice of these countries is underpinned by similarity in religion, culture, resource context and degree of exposure to the Western influence and hence it would be interesting to examine similarities and differences in the main issues this thesis set to study. The research context of Gulf also typified by an increasing level of interest and application of *Shariah* law in business and management practices. There is also an increasing interest by firms and managers of the Gulf countries to seek to acquire modern, up-to-date knowledge, processes, best practices and procedure which align with advances in globalisation and to attract investment to these countries. One of ways of achieving this objective would be engaging in M&A activities with firms of foreign origin. This study thus seeks to examine the influence of sharia CG principles on cross-border M&A between Islamic financial companies in these three countries and non-Islamic countries from the Western countries.

### **3.6.2 Research Sample Selection**

As explained above the total of 15 financial institutions – 9 banks and 6 insurance companies - were chosen using multiple case study approach. As the three selected countries have robust and dynamic financial sector, it was decided that three banks and two insurance companies to be selected as a case study organisations from each of the three countries.

Research sample normally consists of individuals, organisations or specific cases of research interest (Ruane, 2005). Non-probability sampling approach is widely used in business research if the research objectives and questions are likely to be addressed using qualitative research approaches (Zikmund et al., 2012). According to Schreuder et al. (2001) and Kothari (2004) in non-probability technique, there is no equal chance for population to be selected and random selection is not necessary given the nature of specific purposes of research. There are four main types of non-probability sampling: convenience, quota, snowball and judgmental (Bryman; 2012). It is important to bear in mind that sampling is determined by the nature of the study purpose, research aims and research questions (Saunders et al., 2007).

It is worth to discuss in brief each type of non-probability sampling techniques so as to make a case on how one or more of these techniques were used in this study. Although the techniques of non-probability sampling are critiqued because they do not allow the generalisability of the study findings (Buckingham & Saunders, 2004; Bryman, 2008). In addition, they may lack 'scientific rigour', however, they provide rich descriptions and invaluable insights into the issues under investigation.

Purposeful sampling was deployed in this qualitative research for the identification and choice of information-rich, typical, cases (organisations and interviewees within these organisations) in order to address the research objectives and research questions. The purposive sampling method requires the researcher to choose the most appropriate objects based on their knowledge and ability to answer the research questions to meet the research objectives (Saunders et al., 2007). Therefore, the choice of the respective Islamic companies was based on some characteristics such as their size in the industry, insider experience, and activeness in dealing with cross-border M&A. In terms of approach used to select interviewees within the purposively selected 15 financial companies, the researcher searched contact information from the organisations' website and other appropriate sources and then sent an email to the prospective interviewee in the respective positions/roles to request their participation in the research. The email sent outlined the purpose of the research, the time it takes, the relevance of the research and then requested their participation in the research. It did not contain the exact

interview questions, however, where it is impossible to meet them or arrange interview but the interview questions were sent in to some of them who wished to have them before the interview took place.

Snowball technique has attracted qualitative researchers' attention over the years. It is argued that snowball is a form of convenience but is different as the researcher makes initial contact with a small number of subjects to participate in the study (Goodman, 1961; David & Sutton, 2004; Ruane, 2005; Bryman, 2008). For this research, following snowball sampling technique, some participants were referred to the researcher by business and academics contacts, friends and family. At the first week, trying to reach the referrers through phone number was unsuccessful, an email was sent through and effort was made to contact the intermediate person that helped to facilitate the arrangement of the interviews. In addition, the researcher asked for assistance from the initial subjects to help to get others with a similar trait of interest that was interviewed for this study. The researcher personally approached the target participants and scheduled appointments for the interviews. Due to the religion connection with this research that made it difficult to reach some participants easily such as *Shariah* scholars.

Snowball technique that employed in this study helped to identify the individuals mentioned above (Bryman, 2008). However, there are disadvantages of this method such as the first selected participants have strong impact on the sample and thus the results. It is heavily reliant on the skills of the researcher to identify the appropriate participants (Saunders et al., 2009). To overcome the limitation of the snowball sampling, the researcher selected subjects based on their knowledge and professional judgment as well as from different positions and professional backgrounds.

Convenience sampling is where the subjects of the study are selected due to their accessibility and availability to researchers (Bryman, 2008). Another non-probability sampling technique is quota sampling. It is rarely employed in social research and commonly used in commercial and political research. It divides the population into

categories such as gender, age groups and region of resident. This type of sampling aims to reflect people in terms of relative proportion in each category. In this case, the selection of individuals is not random as it depends on the researcher decision to choose the people who fit the research purpose. Whilst quota sampling was not used in this study, convenience sampling of interviewees was used in a few cases but the chosen subjects had relevant and sufficient knowledge and experience.

Given the focus and the objectives of the thesis, it was imperative to follow credible and trustworthy techniques in selecting respondents from the purposively selected 15 companies. The combination of purposive, snowballing and convenience sampling techniques were used to approach interviewees from the selected companies. As issues under investigation required tapping into knowledge, experience and perception of respondents on *Shariah* CG principles and how they were understood and practised as well as the legal structure and the use of *Shariah* compliant financial instruments in the process of M&A, three types of respondents were identified (Hair et al., 2007; Sekaran & Bougie, 2010). Overall, 40 interviewees were conducted with the three group of respondents: *Shariah* board members/scholars (15), legal advisors (12) and senior managers (13) (see Tables 3.2 and 3.3 below for details).

**Table 3.2 Profile of Respondents**

Companies	Saudi Arabi	UAE	Kuwait	Total
Banks	10	7	5	22
Insurance	7	6	5	18
<b>Total</b>	<b>17</b>	<b>13</b>	<b>10</b>	<b>40</b>

Of the 40 interviewees, 22 work for the 9 banks and 18 for insurance companies selected for this study. The above table also shows that 17 respondents were interviewed in Saudi Arabia followed by 13 in United Arab Emirates and 10 in Kuwait.

**Table 3.3 The Participants of the Interviews**

<b>S/No</b>	<b>Participants ID</b>	<b>Organization</b>	<b>Responsibilities</b>	<b>Experience</b>
1	P1-Ins-SA	Insurance	Director of Legal Department	8 years
2	P2-Ins-SA	Insurance	Director of Compliance Department	7 years
3	P3-B-SA	Bank	Lawyer & Councillor for Commercial & Financial field	20 years
4	P4-B-SA	Bank	Consultant for Governance	6 years
5	P5-Ins-SA	Insurance	Legal Advisor	9 years
6	P6-Ins-SA	Insurance	<i>Shariah</i> Board Member	13 years
7	P7-B-SA	Bank	Head of Legal Affairs	11 years
8	P8-B-SA	Bank	Head of Law Department	3 years
9	P9-B-SA	Bank	Lawyer Managing M&A	7 years
10	P10-B-SA	Bank	Lawyer for Managing M&A	10 years
11	P11-B-SA	Bank	Manager for External Deals	21 years
12	P12-Ins-SA	Insurance	Lawyer of M&A Deals	6 years
13	P13-Ins-SA	Insurance	<i>Shariah</i> Board Member	10 years
14	P14-B-SA	Bank	<i>Shariah</i> Board Member	12 years
15	P15-B-SA	Bank	<i>Shariah</i> Board Member	20 years
16	P16-Ins-SA	Insurance	Manger of M&A	9 years
17	P17-B-SA	Bank	Manager of M&A	11 years
18	P1-B-UAE	Bank	Regional Manager	14 years
19	P2-Ins-UAE	Insurance	<i>Shariah</i> Compliance Manger	3 Years
20	P3-Ins-UEA	Insurance	Legal Councillor	14 years

21	P4-Ins-UAE	Insurance	Manager of M&A	10 years
22	P5-Ins-UAE	Insurance	<i>Shariah</i> Compliance Manger	9 years
23	P6-B-UAE	Bank	Manager of M&A	6 years
24	P7-B-UAE	Bank	<i>Shariah</i> Scholar	15 year
25	P8-B-UAE	Bank	Manager of M&A	13 years
26	P9-B-UAE	Bank	<i>Shariah</i> Board Member	15 years
27	P10-Ins-UAE	Insurance	<i>Shariah</i> Board Member	10 years
28	P11-Ins-UAE	Insurance	<i>Shariah</i> Scholar	8 years
29	P12-B-UAE	Bank	<i>Shariah</i> Compliance Manger	6 years
30	P13-B-UAE	Bank	<i>Shariah</i> Scholar	11 years
31	P1-Ins-KW	Insurance	Manager of M&A	6 years
32	P2-Ins-KW	Insurance	External Deals Manager	30 years
33	P3-B-KW	Bank	Compliance Manager	6 years
34	P4-B-KW	Bank	<i>Shariah</i> Board Member	6 years
35	P5-Ins-KW	Insurance	<i>Shariah</i> Compliance Manager	20 years
36	P6-B-KW	Bank	Manager for M&A	10 years
37	P7-B-KW	Bank	<i>Shariah</i> Compliance Manager	8 years
38	P8-Ins-KW	Insurance	External Deals Manager	10 years
39	P9-Ins-KW	Insurance	<i>Shariah</i> Board Member	12 years
40	P10-B-KW	Bank	Managers for M&A	10 years

**Key Guide:**

P-B-SA: Participant from Banking sector of Saudi Arabia.

P-Ins-SA: Participant from Insurance Sector of Saudi Arabia.

P-B-UAE: Participant from Banking sector of the United Arab Emirates.

P-Ins-UAE: Participant from Insurance sector of the United Arab Emirates.

P-B-KW: Participant from Banking sector of Kuwait.

P-Ins-KW: Participant from Insurance sector of Kuwait.

These selected respondents play key roles in organisational decision-making, oversight, in interpreting business environment and the context in which these firms operate. For example, legal advisors entrusted with advising business organisations on issues regarding laws, rules and regulations, including *Shariah* law and principles, which have impacts on the business organisations. *Shariah* board members and *Shariah* scholars, for example, act as interpreters of sharia law and ensure whether the business organisations comply with them. Senior managers in these organisations are responsible in leading and managing these financial institutions to achieve organisational goals. Hence, the three groups of interviewees selected for this study were appropriate to address the research issues under investigation. The diversity of roles and positions of these interviewees meant that the study was able to uncover contrasting and complementary perspectives on the issues under investigation and this in turn enhanced the credibility, trustworthiness of the findings. The above table also shows that all the sample respondents had rich work experience, thorough knowledge of the context, and relevant role and these features combined helped the gathering of appropriate data.

Each research participant was interviewed on 25-30 questions about the impact of *Shariah* principles and cultural influences on the formation of cross-border M&A. The total of 40 respondents were interviewed from the three Gulf region countries (see Table 3.2 and 3.3 above. Two categories of participants were interviewed - internal and external participants - the same questions to compare the responses in order to increase the validity of the research outcomes.

The sample size ensured the researcher had a sufficient number of companies and interviewees from different countries within the region. The research outcomes can be used to draw implications on how different Islamic countries which are not culturally too diverse can have variations in the implementation of *Shariah* principles in their various businesses.

### 3.6.3 Process of Data Collection

Since there is need to coordinate with companies located in multiple locations, the researcher expectedly had delays in the research process. The data collection lasted for 9 months, between December 2013 and August 2014. As part of this process, the researcher had to explain and provide clarifications about the purpose of this study as well as ensuring the participants' names was changed to maintain confidentiality (Sieber, 1992; Gullemin & Gillam, 2004).

Following their selection and their agreement to participate in the research, a phone call was made to provide brief information about this research and what they will be expecting during the interview. The interviews were conducted in the respective countries, and in the organisation's office or anywhere else as agreed *a priori*, except if otherwise requested by the interviewee. The option of language was kept open between Arabic and English, the interviewee was given the chance for them to choose which language they are comfortable with, but many liked Arabic except some managers who have a good grip of English language. The interviews lasted for not more than one hour each. Before the beginning of the interview, the researcher explained the objectives of the research, and the rights of the participants and that the data will be used for research purpose only (Wiles et al., 2008).

A small portable device was used for recording in order to prevent any loss of valuable information or any change in the actual interview (Saunders et al., 2007). The researcher used the phone numbers and emails provided by the interviewees to keep in touch in case of any further information or any clarifications are needed. The data collection process ensured the confidentiality and anonymity of the interviewees to comply with research ethics. All records protected to ensure that the true identities of the participants were not shared in the research to protect research participants from harm; instead codes were used to represent the opinions of the research participants (Sieber, 1992; Baez, 2002).



The interviews were transcribed verbatim by playing the recorded interview and putting it in a print, some interviews recorded in Arabic and then translated to English and effort were made to ensure that all the transcription error had been corrected and the accuracy in the translation. These were done by using transcribers which were proficient in both English and Arabic languages to ensure the accuracy of translation.

### **3.7 Designing Interview**

Malhotra & Birks (2000) stated that data should be collected based on specific needs of the research purposes. In addition, it is important to have a plan for data collection based on the areas of interest (Saunders et al., 2007; Ritchie et al., 2013). The researcher designed three sets of questions for each category; managers, lawyers and *Shariah* Board members of the target companies in order to investigate the impact of *Shariah* principles on M&A between Islamic and non-Islamic countries. The questions were constructed in such a way as to enable the collection of relevant and appropriate responses from the interviewees. All the respondents were asked similar demographic profile and common questions. However, depending on the type of audience, the questions were designed to know the influence of the *Shariah* law on their job responsibilities when dealing with cross-border M&A on a regular basis.

Further questions were asked to help address issue relating to various leadership styles; managing organisational and people's cultural differences as well as managing financial and legal risk. The interview questions followed by prompt questions provided an in-depth investigation of the research issues that might be relevant to the study (Hair et al., 2007; Bryman, 2008). The questions extracted from the literature review and were flexible to work with different participants (Saunders et al., 2007).

The table (3.2) below indicates the major themes from literature review and how they were used to develop the semi-structured interviews. In addition, the researcher further explained the rationale behind the interview questions for each of the categories, and

how each question has a specific outcome that was used to achieve the research objectives.

**Table 3.2: Major Themes from Literature Review**

Theme	Remarks	Existing Literature
Corporate Governance	To find out information on the adoption of CG code of practice in Islamic companies in the Gulf countries.	Shleifer & Vishny,1997; Becht et al., 2003;Huse, 2005; Haniffa& Hudaib,2006;Claessens, 2006; Grais& Pellegrini,2006; Baydoun et al., 2012; Al-Musalli& Ismail,2012.
Corporate Governance Mechanisms	To examine the difference between Islamic companies in the Gulf and non-Islamic companies in Western countries in terms of CG mechanisms in respect to cross-border M&A including disclosure and transparency, Board size and characteristics, ownership structure, dual chair and internal and external auditors.	Ho& Williams, 2003; Abbott et al., 2003; Naser&Nuseibeh 2003; Aguilera & Dencker, 2004; Chahine, 2007; Fan & Wong, 2005.
Incorporating Islamic Principles in the Business	To examines whether the adoption of Islamic principles of CG can restrict business expansion through international M&A	Chapra & Ahmed, 2002; Iqbal& Mirakhor,2004; Lewis,2005; Choudhury &Hoque, 2006; ElGamal, 2008; Safieddine,2009; Hasan,2009; Abu-Tapanjeh, 2009; Farook et al.,2011; Elasrag, 2014.

Cultural Influences:	To explore the variations in the culture which can be a deciding factor in the expansion of the businesses from the local border to the international borders. The country to country cultural variations would result in different business policies, leadership styles and management practices of the companies.	Khanna et al.,2000; Zollo& Singh 2004; Stahl & Voigt, 2008; Haniffa & Cooke,2002 Licht et al., 2005; Haniffa & Cooke, 2005. Sabi, 2015.
Need for <i>Shariah</i> Compliance	To explore the implementation of <i>Shariah</i> law in Islamic companies within the selected Gulf countries and the impact of different interpretation of <i>Shariah</i> by scholars. Also, to investigate the status of the compliance and how likely they follow all the regulations set forth by the <i>Qur'an</i> , <i>Sunnah</i> and if not why they do not follow these rules in their line of business.	Sundararajan & Errico, 2002; Sole, 2007; Hasan& Laws, 2007; Choudhury & Alam,2013; Paino et al., 2011; Khalid, 2013; Maswadeh, 2014; Derigs & Marzban, 2008; Rezaee, 2011.
Islamic Corporate legal Structure	To find out how the legal structure of the Islamic companies is influenced by the national legal system, which in case of Gulf	Ararat & Ugur, 2003; Angell, 2006; Alkhamees, 2013; Grassa, 2013; Grassa & Matoussi, 2014; Bhatti & Bhatti, 2010.Elasrag, 2014;Shafii & Salleh,

	countries is quite complicated as it reflects history, religion and traditions of each country. It also manifests the principles and codes the company is bound to follow in the conduct of their business.	2010; Matoussi &Grassa, 2012.
Islamic Financial instruments	To find out the Islamic alternatives for the investors to either expand their businesses through the M&A or to start new business. How the Islamic financial instruments affect the business decisions, and the challenges they faced in the negotiations with their counterparts.	Usmani, 2002; El-Gamal, 2000; Jaffer et al., 2012; Ayub, 2009; Saeed & Salah, 2014; Al-Amine, 2008 Ahmad et al., 2009; Msatfa, 2011

### 3.8 Pilot Study Details

The researcher conducted a pilot study in order to test effectiveness/feasibility of the data collection instruments before using them. This helped the researcher to identify areas for clarity and to minimise the misunderstanding or misinterpretation of the questions during the actual data collection process (Denscombe, 2010).

According to Bryman (2008) it is always beneficial to conduct a pilot study before proceeding to the actual interview. After receiving responses, it is usually difficult to resend the questions to respondent or get them to clarify their response in case they do

not understand the question (Berg et al., 2004). In addition, because it comes at the early stage of the research to test the research objectives or interview questions, it might mislead the research if the respondents do not understand the question very well or do not have enough experience in the area. However, there are advantages attached to it, as it could provide prospective area of research on the chosen topic and help prevent deadlock/dead end research (Christensen et al., 2011). So, doing a pilot with similar population provided this researcher with opportunity to modify and change some questions before administering them during data collection. The possible rebuttal questions can also be found, and having these answers ready in hand, will show the researcher preparedness on this subject when the interviews are done with target people of the suggested firms. Pilot study helped the researcher to be prepared for the big day (Van Teijlingen & Hundley, 2002).

Questions were discussed with the different categories of interviewees and their responses provided the researcher with an opportunity to practice, using it to spot any problems that emerged in potential interviews; which led to more sense of confidence. The researcher came up with the final interview questions based on the iterations through pilot study done in 2012. The key insights and feedback received from the pilot study helped the researcher to formulate the right interview question set for each category accordingly.

In addition, it also helped the researcher to identify areas that respondents were not very comfortable with. During the pilot study, the researcher attended two conferences, one in Saudi Arabia (The Islamic finance news conference 12&13 November 2012), and the other in UAE (KPMG'S 2012 Masa tax conference 26<sup>th</sup> of November 2012). These two conferences witnessed a large convergence of industry personnel from different Gulf countries, sharing knowledge on Islamic CG and M&A and other financial updates on CG. The researcher noticed that a number of experts attended the conference and interviewed nine experts in total for the pilot study. The participants who voluntarily submitted themselves for the interviews as part of the pilot study are tabulated below.

**Table 3.3: Pilot Study Participants**

<b>Participants ID</b>	<b>Position</b>
P1-UAE- Audit Firm.	Assistant Manager- <i>Shariah</i> Audit
P2-SA- Audit Firm	Director, <i>Zakat</i> & Tax
P3- SA- Audit Firm	Director, corporate Tax
P3-SA- Islamic Research & Training Institute	Research Assistant
P4-SA- Audit Firm	Director, <i>Zakat</i> & Tax
P5-UAE-Bank	Regional Head
P6-Bahrain- Law Firm	Legal Advisor
P7-SA- University	Scholar and Expert in Islamic Finance
P8- Oman-University	Professor in Islamic Economics and Finance
P9-KW- Investment Co	Vice Chairman

At the conference location, quick interviews were conducted which included lawyers, academics and managers, some of the manager respondents indicated that there is little or no effect of *Zakat* on cross-border M&A. On the other hand, they added that there could be some issues which might not yet be in the limelight because cross-border deals have not yet been practiced there for a long time, implying that it is an emerging area, pointing out that *Zakat* is not a CG issue but a financial issue. Some lawyers said there could be issue but because of limited exposure and experience, they were still trying to learn from other developed countries. The academics agreed that it is an issue but no one has really researched into this area and the Islamic finance has not been built to this level because the Government did not build the financial institution and Islamic finance research institutions that could look at this area. The respondents' views were taken into consideration and appropriate adjustments made.

The outcome of the pilot study is that the variation in the interview questions for each category ensured that the research subjects were exposed to the right questions. The researcher considered the pilot study responses and made adjustments on the initial aim of this study, which was looking at the impact of *Zakat* (Islamic tax) as a part of Islamic principles on cross-border M&A. *Zakat* is an Islamic instrument of law, which is localized in Gulf countries, as such it could reduce the scope of this research since it would require much more extended study which might not be available in academic format, particularly when the Muslim world never thought of such policy-theoretic idea, except for banks to have collected and disbursed *Zakat* out of their *Zakat* fund. However, there are hardly any academic developments on Islamic CG and cross-border M&A.

Formalizing such an interrelated study between *Zakat* and cross-border M&A in Gulf countries is an interesting project, however at this time only the theoretical part can be done, neither data can be found nor any programs in action that can be given academic attention, also, there are not enough evidence of failed transaction due to *Zakat*. Therefore, the research scope was broaden, finding out instruments of CG that plays important role in cross-border M&A to make a comprehensive study in Islamic finance. This process reduced the costs and time that could arise by identifying the issues that mitigated before the actual data collection.

### **3.9 Interview Confidentiality**

With regard to collecting primary data, which was undertaken for this study, the access issues involved were whether the researcher will be permitted to carry out data collection in the selected target companies in which *Shariah* CG have taken place and whether the target participants will adhere to a focus interview with the researcher. The literature reviewed formed a critical aspect of data collection (Mays & Pope, 2000).

There is no compensation for the participants involved in the qualitative research. The responses of the research participants are the property of the researcher for a period of time, and henceforth the data will be public, and accessible to anyone. The responses of the research participants are used anonymously without any real names in the research for confidentiality. Names of the participants were coded in order to maintain the anonymity of participants and make it difficult for anyone to identify them in the research data analysis part (Kaiser, 2009).

With regards to the collection of secondary data, access issues are not much involved compared to primary data. However, since corporate documents on cross-border M&A and CG are needed, the researcher wrote a formal letter addressed to specific personnel concerned (i.e. Manager, Lawyer etc.), requesting for access to these documents. The participation of well-known industry experts in the qualitative research gave greater authenticity and credibility to the study (Bryman, 2012). All the confidential documents received from the participant were not shared with anyone without written permission from the participant for its use. No access issues are involved in collecting online sources, unless the data are available only upon purchase, of which the researcher may decide to find another similar source or purchase it online (Guillemin & Gillam, 2004).

### **3.10 Interview Trustworthiness**

Qualitative research use key methods such as credibility and dependability to achieve the trustworthiness of interviews (Guba & Lincoln, 1995; Shenton, 2004; Graneheim & Lundman, 2004). Credibility is defined as the maintaining consistency of the participants' perspectives during the interview process to achieve transparent outcomes (Morrow, 2005). Researcher's understanding of the phenomena under investigation should be of interest from the participant's perspective (Patton, 1999).

Dependability is concerned with whether the findings are accurate and aligned with the research aims, the interviewees and readers. This can be achieved by avoiding any tendency or prejudice toward participants and equal and fair presentation of the aim of



the research to the interviewees (Golafshani, 2003). The researcher developed an early familiarity and understanding about the organisations under study before collecting data from participants to establish a relationship of trust between the parties (Silverman, 2001). The researcher contacted the participants and they share some documents and sources before the interviews and they invited the researcher to conferences.

This study ensured that the data collected are reliable and accurate as each participant was given opportunities to refuse not to provide data freely. In addition, credibility was achieved through further clarification and interpretation in the data analysis chapter when the responses remained vague. However, the researcher's and the respondents' interpretations were separated. The outcomes of the research have key insights highlighted from the experiences of participants and can be a trusted source of information. The researcher used the raw data from the interviews, which also became the researcher's property for further analysis in the future.

Furthermore, the participants' background, qualifications and experience of the research topic are key factors that ensure reliability of the data collected (Shenton, 2004). The researcher proposes the use of triangulation that involves interviewing different people from different categories differently. This framework is used to shortlist the key behavior traits of three target groups towards the cross-border M&A and Islamic principles on these strategic relationships with non-Islamic countries, which are to be considered in order to understand the ways in which participants have to ensure an understanding of the problems (Johnson et al., 2007; Creswell et al., 2011).

### **3.11 Data Analysis**

The analysis step is a continuous process of data collection; however, collecting data by itself will not achieve the research objectives without analysing and interpreting the data collected (Miles & Huberman, 1994; Spiggle, 1994; Thomas, 2006).

Qualitative data analysis such as interviews analysis follows a step-by-step procedure that involves preparing data by going through the process of transcription and writing word by word of the recorded interviews (McLellan et al., 2003; Halcomb & Davidson, 2006). Powell & Renner (2003) suggest three steps to qualitative data analysis. First, familiarization with data; second, generating initial codes, identify themes capturing codes, reviewing themes, category formation; third, establishing patterns and relationship between themes through formation of core categories for an overarching analysis. Similar suggestion also made by Attride-Stirling (2001) who outlined data reduction strategy for meaningful analysis. The procedure involved developing codes and themes from the empirical data which lead to constructing sub-categories and core categories in order to properly analyse data (Hair, 2007; Sekaran&Bougie, 2010).

First stage of the process is reading and reviewing of the interview transcripts to group the content into codes and this can be focused on repeated words phrases, cases and concoction to gain evidence for the research question from literature review and interview transcripts (Bryman, 2008; Grbich, 2013). An example of the first order codes and related description of the code from the interview transcripts are shown in Table 3.4 below. Second, from the codes, the researcher develops themes which consist of two or more codes and associated supporting texts (Welsh, 2002). Thirdly, the sub categories were grouped into core categories for ultimate write up and analysis. This approach enabled the researcher to understand the findings from all three categories by mapping concepts and themes identified (Attride-Stirling, 2001; HesseBiber & Leavy, 2010).

The codification process of themes and codes can be developed from the literature or can be generated from the data collected (Glaser, 1965; Saunders et al., 2007; Saldaña, 2015). However, the researcher identified them iteratively between the literature and the data collected. The process of qualitative analysis in this study was done inductively as the researcher started with huge data collected (interviews) and from the content, the researcher determined any pattern (themes, concepts) by using emergent framework and then find relationships. This tactic was based on creating a table of themes and codes for each interview (see Figure 3.1).

**Table 3.4: Main Themes and Codes Transcription**

<b>Themes</b>	<b>Codes</b>
Obstacles	Cultural differences
	Control on decision making
	Complex procedures & regulations
	Lack of transparency
	Quality of information
	Conflict of interest
Key Drivers	Large profits
	Business opportunities and experience
	Competition in home country
	Economic boost of home country
	Culture and values reinforcement

NVivo has been designed to aid the analysis of huge-text used in qualitative research, as it allows deeper analysis and provides more developed tools to visualise data (Patton, 2002; Gibbs, 2002).

NVivo software thus was used in the process of constructing code, themes and categories (Strauss, 1987; Joffe& Yardley, 2004). NVivo used in coding, theory building, analysis of data which helped the understanding of the research problems (Denardo, 2002, Bazeley& Jackson, 2013). It allowed the researcher to replace ‘paper and pen’ technique by data management and analysis tool.

NVivo was used in this study as it provides many advantages. First, it provides more flexibility in the ways in which to categorise rich-text data and improves the quality the generated results. Second, it helps to reduce the time and efforts that are used to analyse data manually. It also helps to identify trends and cross-examine information to discover the most important and relevant themes to the study to produce better

conclusion (Wong, 2008). Furthermore, it has a capacity to analyse, classify and categorise massive data derived from interview transcripts, surveys, notes and published documents (Welsh, 2002). Finally, it also helps to create stunning graphs and models to present the explored relationships between concepts (Bazeley & Jackson, 2007). Before using NVivo, the researcher participated in appropriate workshops and training courses to gain the required skills to use the software. This software has been selected because it enabled the researcher to control large amounts of data and to create model for themes and sub-themes (Gibbs, 2002).

There are many approaches under qualitative research that can be adopted for analysing qualitative data. Some of these qualitative data analysis approaches include thematic analysis, content analysis, framework analysis, grounded theory analysis and thematic discourse analysis (Saunders et al., 2007; Bell & Bryman, 2007; Sekaran & Bougie, 2010).

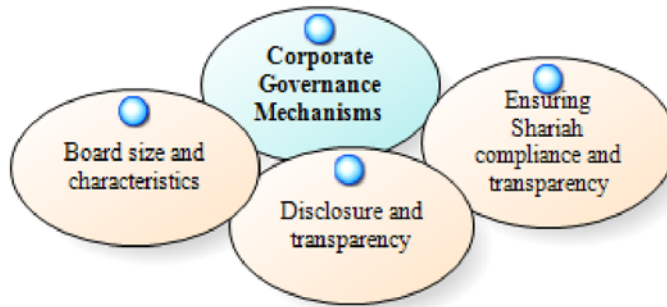
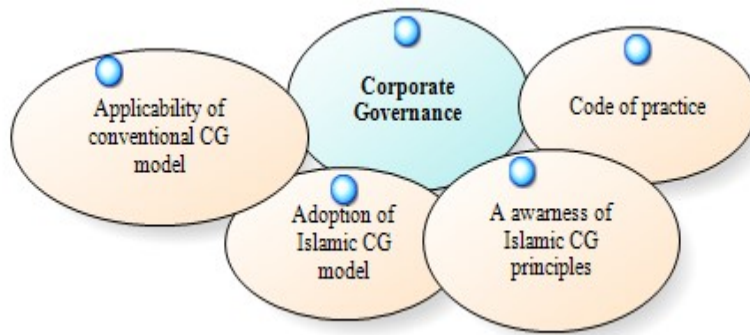
The transcribed data were analysed using thematic analysis. According to Smith & Firth (2011), thematic analysis is generally adopted in circumstances where the research plans to determine themes from the data that has been collected. These themes primarily refer to blueprint of data that outlines a phenomenon that is related to the research question. Easterby-Smith et al. (2012) specified grounded theory as an approach in which the research is highly flexible and research design is moulded in accordance to collected data and continuing analysis of data. They also outlined framework analysis as an approach in which the researcher resorts to an extremely focused strategy to determine the blueprint of data. Such research analysis is generally commissioned. According to Krippendorff (2012) Content analysis approach is primarily adopted in circumstances where the research seeks to compare and contrast answers from respondents in order to meet research objectives.

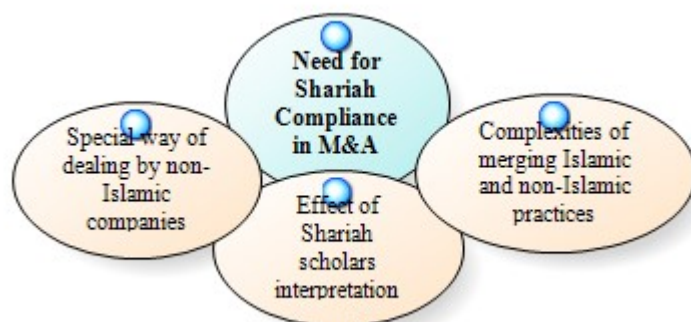
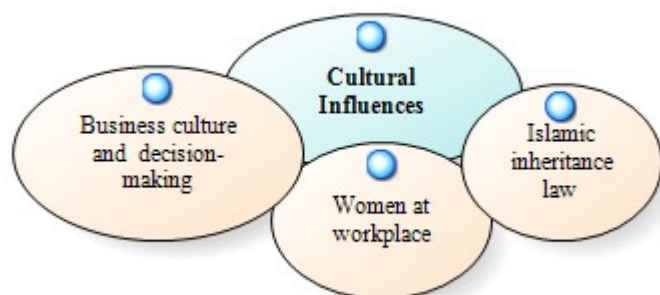
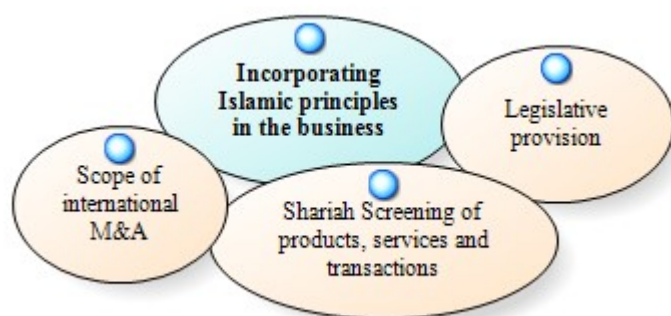
However, thematic analysis was chosen for the analysis of the data gathered as a way to aid the understanding of the context of the data, and draw out inter links between data

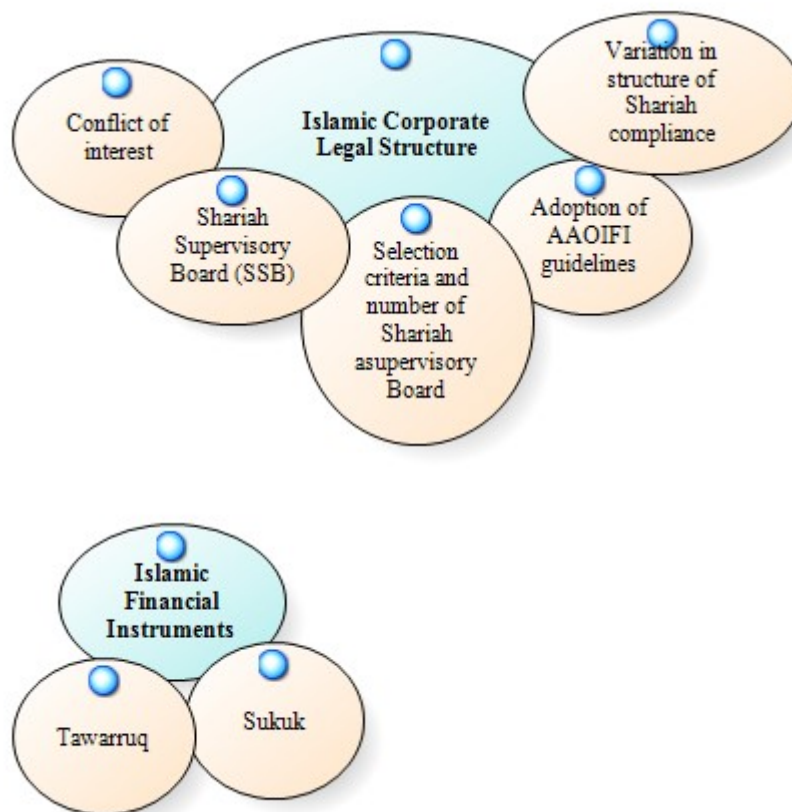
from a number of sources to discover in-depth meaning of the participants (Bennett & Elman, 2006; Ritchie et al., 2013). This is in particular needed in order to ensure that the data analysis can be improved over time (King et al., 2004). Further, this approach provides an opportunity to interpret themes from data which other approaches fail to do. In addition, it provides researchers with greater flexibility and provides options to enlarge the scope of study of individuals' understanding (Smith & Firth, 2011). The researcher used the label thematic analysis that follows a process sequentially used in qualitative research, to gather insights on the research interview data or focus group sessions (Tesch, 2013).

The use of NVivo software in the analysis generated sub-themes and main themes which were used for the analysis of the interview data in well-organised manner. Overall, seven core themes and 23 sub-themes were identified through the process of coding and thematising as shown in Figure 3.1 below. Example of core themes included 'corporate governance mechanism' with sub-themes 'board size and characteristics, disclosure and transparency and ensuring *Shariah* compliance and transparency'. Detailed analysis and interpretation of the core themes and sub-themes are presented in Chapter Four.

**Figure 3.1: Themes and Sub-Themes**







However, thematic analysis has a few limitations. By using thematic analysis, the research undertaking research in higher phases becomes difficult as it provides high degree of flexibility. Further, it restricts power of elucidation of the researcher, thus having adverse impact on research analysis and findings (Joffe & Yardley, 2004).

### 3.12 Ethical Considerations

Cohen et al. (2013) stated that appropriateness of topic, methods, design, confidentiality, examination and distribution of findings should be discussed with relative sincerity, sensitivity, integrity, precision and impartiality in order to improve the ethical approach of research. It is important for a researcher to consider the following areas: any potential harm to participants; any lack of consent; any invasion of privacy and any deception involved (Miller et al., 2012). These are deemed to be very



important to ascertain that any research work has been undertaken within the confines of the rules and regulations guiding research activities in any given environment.

In order to ensure the authenticity and ethical consideration of the research participants, the researcher interviewed only people who are above eighteen years of age, and have the ability to express their thoughts as guaranteed by the prevailing laws. Also, because this study was closely related to religious practices, sufficient caution was applied in conducting interviews in order not to hurt the interviewers' sentiments about their religious beliefs. To ensure consent to participation prior permission was sought from the participants. Furthermore, the researcher obtained permission to record the interviews from the different participants to avoid a betrayal of trust, so only recorded after due permission was secured from participants. No real names and only codes are used in this research; this ensured confidentiality of the research participants. Moreover, the researcher abided by the rules governing research within DMU.

### **3.13 Chapter Summary**

This chapter presented and justified systematically the research methodology used in conducting this study. The 'Research Onion' of Saunders et al. (2007) was used as a guide to structure the presentation but more importantly several relevant and credible sources were used to justify the chosen research methods and research design. Given the research purpose and research objectives, an interpretivist research philosophy and an inductive approach informed this research. Empirical data was collected from the multiple case studies comprising nine banks and six insurance companies in the three Gulf countries and semi-structured interviews with 40 respondents to address the research question regarding the influence of the *Shariah* principles on cross-border M&A. The data was analysed using NVivo software following thematic analysis procedure. All the research ethical considerations were observed. The next chapter presents findings and analysis.

## **CHAPTER FOUR: FINDINGS AND ANALYSIS**

### **4.1 Introduction**

This chapter presents the results and analysis of qualitative data gathered through semi-structured interviews. The results and analysis are presented in such a way as they enable to answer the research questions. The thematic data analysis produced seven core themes anchored by both the empirical data and the reviewed literatures and the chapter is organised accordingly. Following this introduction, results on corporate governance is presented. This is followed by corporate governance mechanisms in section three. Section four and five present findings regarding incorporating Islamic principles in the business and cultural influences, respectively. Results on need for *Shariah* compliance, Islamic corporate legal structure and Islamic financial instruments are discussed in sections six, seven and eight. Brief chapter summary is presented in final section.

### **4.2 Corporate Governance**

One of the key themes emerged from the data analysis was corporate governance. This core theme is captured by the sub-themes including the adoption of CG models, code of practice, awareness of CG principles, and applicability of conventional model. This section analyses similarities and differences in the perspectives of respondents regarding the Islamic and conventional CG.

#### **4.2.1 The Adoption of CG Model**

The concept of CG has been elaborated in these themes with respect to emphasis on the similarities and differences between the conventional and Islamic CG. This sub-theme emerged from the qualitative analysis of managers' responses to interview question 11, from appendix 3 and questions 4, 5, and 8 from appendix 5. This study provides information on the adoption of CG code of practice in various Islamic companies, especially in banking and insurance sectors. The CG of non-Islamic companies in terms of CG does not have many differences with the Islamic CG. One of the respondents from insurance sector reported that:

*“CG concept is not a totally new concept in my opinion, most of the rules and regulations we used to operate our business in SA followed the Anglo-American model of CG both the Islamic and non-Islamic companies, however, the Islamic companies ensure that the Islamic principles are enshrined in the model. The introduction of the CG code in Saudi companies have even led to Islamic scholars discussing about the adjustment or modification in the Anglo-American model whether it is in line with Islamic principles or not”. [P1-Ins-SA]*

The common consensus among the many respondents is that in all the three selected Gulf countries, are willing to adopt any model of CG as long as they can make adjustments. Evidence shows that the SA company act was derived mainly from British company Act (Hussainey& Al-Nodel, 2008; Al-Matari et al., 2012) with implications for nature of the CG being adopted. As discussed in the literature review, the Anglo-Saxon model has its origin in the UK, US, Canada, Australia and many countries have adopted the model (Davis, 2002; Garcia-Meca& Sanchez-Ballesta, 2009). This suggests that the conventional CG have relevant principles such as accountability, transparency, responsibility that support the successful implementation and sustainability of CG (Abdul-Rahman & Bukair, 2013). The implication is that the three selected Gulf countries are likely to adopt the conventional CG as principles are to a greater extent similar to Islamic principles. Furthermore, the Gulf companies have no CG index model

in the whole region (AL-Malkawi et al., 2014). Also many researchers have emphasised the need of operating *Shariah* principles in Islamic companies as Hasan (2011, p.1) noted “*Shariah* governance is peculiarly exclusive and unique to the Islamic system of financial management while affirming the need for a sound and efficient *Shariah* governance system as a crucial portion of CG in Islamic financial institution”. This indicates that the Islamic companies will be enshrined Islamic principles in conventional CG models.

Despite the similarities of the practices of the conventional and the Islamic CG, however, there are contextual differences such as social norms and religion, which may have some negative impacts on the selected Gulf countries CG practices that may lead to ineffectiveness of CG code of practice (ROSC, 2009; Baydoun et al., 2012). This could suggest why the three selected countries are willing to make an adjustment in any CG model, as they recognised that the conventional CG code principles are not informed by the Islamic principles. This indicates that one of the main objectives of the Islamic countries and companies is to examine the differences that are hidden or noticeable in the conventional model and propose for an adjustment. They may affect the way non-Islamic companies’ deals with Islamic companies in the cross-border M&A. However, from the learning theory perspective, firms that interact or enter into business activities in foreign markets, can improve on new learning skills, which is a strong capability that can improve the ability of company innovation, take risk and develop multiple sources of income (Zahra et al., 2002) This could suggest what there should be some sort of flexibility in the adoption of CG models.

In the three selected Gulf countries, the adoption of any CG model is based on the extent to which it enshrines *Shariah* principles due to the strong belief in the Islamic way of life but also due to benefits that will come from morally sound corporate and social practices. However, dealing with the cross-border M&A, this may pose a serious threat for both the Islamic and the non-Islamic companies.

#### **4.2.2 Code of Practice**

This section provides information on code of practices of Islamic CG by Islamic financial companies. The researcher asked the existence of written Islamic CG rules and regulations (Interview question 16, Appendix 3). The consistent response from the many interviewees is that the non-existence of written Islamic rules and regulation on Islamic CG. So, the code of conduct of Islamic companies is influenced rather by the cultural and religious considerations which emphasise philanthropic approach, the well-being of community, the distribution of the wealth through charity and other humanistic actions. For example, one respondent from the banking sector in SA reported that:

*“There are no written codes of Islamic CG; it is mostly derived from the fundamental principles of the Islamic business laws described by the scholars on how to run their business within Islamic boundaries. The advent of conventional CG, shared so many similarities with Islamic business principle such as philanthropic approach, the well-being of community, the distribution of the wealth through charity and other humanistic actions”. [P3-B-SA]*

This indicates that there is no written Islamic rules and regulation as regards to CG; everything is evaluated based on Islamic principles. This observation accords with that of Badah (2014), who noted that there is lack of unified and well-structured CG guiding principles for Islamic financial institutions in the Gulf region. A survey on *Shariah* governance practices in Malaysia, Gulf countries and the UK shows that most of the Gulf countries are not even aware of the existence of the exposure draft of Islamic Financial Services Board guiding principles which is based in Kuala Lumpur, on *Shariah* governance system (Hasan, 2011). The author also noted that Gulf countries prefer less regulatory interference on the market. This could suggest why the selected Gulf countries do not have a written code of practice based on *Shariah* CG.

Despite there are no written code of practices by the Islamic companies in the selected Gulf countries, their practices clearly show features of Islamic principles, as the Islamic *Shariah* provides a common starting point for code of conduct, to reflect the cultural and religious characteristics of the region (Islam& Hussain, 2003). The Islamic practices of Islamic CG have shown much similarity with the conventional CG such as accountability, honesty (Mollah & Zaman, 2015). However, there are also an indication of differences emphasise by researchers. For example, the *Shariah* governance structure differs from the conventional CG such that in *Shariah* the accountability is not only to stakeholders but also to God “*Allah*” (Abu-Tapanjeh, 2009; Widiyanti et al., 2011). Also the proliferation of the business within the community needs to be based on the criteria of the amount of the benefits taken by the local and international community. Islam does not permit the expansion of business activities solely for the benefit of individuals, but it considers the benefit of the whole community. Hence, Islamic financial institutions do not support any type of business exploitation that is unfair to the people or damage the environment. They are required to deal with the society and the environment justly with their stakeholders.

#### ***4.2.3 The Degree of Awareness of CG Principles***

One of the research questions was to understand to what extent the Islamic financial institutions are aware of, and adopt, CG principles. The empirical finding from interview questions 6 and 26 from appendix 5 showed inadequate level of awareness and adoption of CG principles with some level of variations across the three countries. The interviews analysis showed how the employee of Islamic banking and insurance companies are aware of the practice of CG in the three selected Gulf countries. It also emphasises whether the CEO’s and managers commit to the code of conduct or they do to create awareness to the employees. Respondent in SA reported that:

*“Most of the Saudi Companies believe that they are doing quite well in terms of implementing the modified versions of codes of CG, but still they need more regulations. In fact, some people do not understand the CG concept and there is no any known effort or initiative from the Government to increase the awareness about the CG”.* [P5-Ins-SA]

Also, in contrast to respondents from SA, the respondents from Kuwait showed unawareness to the concept of the CG and its code of conduct in Kuwait companies. One of the experts from Kuwait was of the view:

*“The concept of the CG in the Kuwaiti Islamic companies is new, and most of the people working in the industry are not aware of the concept of CG. The latest I can remember, the concept has been talked about from 2012-2013, which means we are not fully aware either Islamic or conventional CG”. [P1-Ins-KW]*

Another respondent showed the agreement with the view of the above respondent by commenting that:

*“As far as the practice and implementation of the code of practices derived from international CG is concerned, I will rate the Kuwaiti companies the lowest ranked companies among the list of companies doing business in the Gulf countries. The debate about the conventional or Islamic CG did not attract the attention of the business people working in Kuwait”. [P10-B-KW]*

The above comments suggest that most companies are aware of the practice of CG in SA and Kuwait but suggest that most of the employees are not fully aware of the concept of CG. This finding is similar to DCCI (2006, p.10), which stated that “awareness of corporate responsibility at management levels is high [...] however; it becomes increasingly apparent that companies are saying one thing and doing another”. This shows that Islamic companies in SA do not fully understand the concept of CG and how it impacts on their organisation performances. For example, Baydoun et al. (2012) stressed there is need for the Gulf countries to access the international capital to fund growth among the region with the aim of becoming the financial and regional

development centre and as a member of the World Trade Organisation (WTO), which will lead the local regulatory agencies to collaborate with international agencies to consequently design new regulatory schemes to improve on CG. In order to fully understand the concept of CG and for its application, there is a need to upskill employees through regular training.

The unawareness of the SA companies' employees may have negative impact on the companies. This is an indication that it is unclear what policy Government has on ground to enforce organisations to create awareness due to enormous benefit that effective CG has. The problems in creating awareness among their employees about the importance of CG could be due to the poor rules and regulations. In comparative survey of CG in the Gulf countries, Hirst (2010) pointed out that the weakness in the law system among the various companies in the Gulf countries need to be addressed if the countries want to become major player in the Middle East and the world. In practice, some Gulf countries have started integrating into the world economic through trade and M&A, thus leading to change in companies' structures and conception. For example, some companies in UAE have engaged in one form of economic or business activities with the global organisations.

A respondent from UAE banking sector was of the view:

*“There is a growing awareness of corporate governance in the UAE and many companies take it as a periodic appraisal exercise to improve their corporate governance practices”. [P2-B-UAE]*

However, it is not clear why the UAE CG framework is not better off compared to SA or Kuwait which have lesser business interactions with the global economy (Saidi & Kumar, 2008). Consequently, based on the CG measurement scale among the Gulf countries, Baydoun et al. (2012) emphasised that in some aspects Kuwait and SA are



better than UAE such as transparency and internal process, while in some aspect UAE is better than Kuwait or SA such as in shareholders right and obligations.

However, from the analyses it was found that the selected countries of the Gulf are not aware of either the conventional or Islamic CG. This unawareness could have a negative effect on the Islamic companies and it could be caused by lack of professional training, lack of commitment by the Government and adequate payment of sufficiently qualified staff (Al-Shammari, 2008). For cross-border M&A this is a very important element for successful engagement with the global economy. However, there are indications that some countries in the Gulf region such as UAE have started merging and acquiring companies. This is an indication that there is possible cross-border M&A between the Islamic companies in the Gulf and non-Islamic companies in the West. To be fully integrated there is need for general awareness and training to understand the importance of CG for easier integration with non-Islamic companies.

#### ***4.2.4 Applicability of Conventional CG Model***

This section explains the aspect of the conventional code of practices, which are of greater concern to the Islamic companies. Majority of respondents to interview question 5 from appendix 5, believed that the conventional CG code of practices require some modifications to be sensitive to Gulf countries cultural values and Islamic religion. They argued that conventional CG principles should be evaluated on the Islamic *Shariah* principles and culture and this may pose challenges in cross-border M& A activities. Such views were, for example, expressed by many respondents from the UAE's banking sector.

*“The CG models adopt by the Western countries and the USA cannot be applied directly to the companies working in the UAE. This is due to the fact that these models do not take into account the geographical and demographic features including the culture and religion practiced by the people of the UAE”.* [P1-B-UAE]

Another respondent from insurance sector seems to support the above-mentioned views: *“I think that there is a real need of improvement in the structure of codes of the practices adopted by the companies running their businesses in the UAE. The practice of good CG cannot be implemented by the UAE based companies with making good allowances for the codes of practice provided the religion and culture of this region. With these modifications and inclusion of key codes of practice from the conventional CG, the Islamic CG can be fully complied with the regional and international standards”*. [P3-Ins-UAE]

Moreover, one of the experts from the UAE viewed the level of implementation of the good CG as:

*“I believe that good CG practices are aligned with the most of the regulations from internationally applied conventional CG practices; the establishment of the CG is very well rooted in the culture of the companies in the UAE. However, the new Government regulations are being introduced to introduce the good religious and culture practices of the UAE to give more stability and soundness to practices in the UAE-based companies”*. [P10-Ins-UAE]

The comments suggest that Islamic companies are willing to adopt conventional CG code of practice but it will be evaluated based on Islamic fundamental principles and culture. The modification is not to sub-standardise the conventional CG but to adjust it so it accommodates the Islamic companies. Similar to this view, Black et al. (2010) emphasised that there is preconceived assumption that “one size fits all” which implies that fair Government practices are universal and any company in any country of the world should be able to apply it. However, Bhatti & Bhatti (2010) saw the need for the Islamic companies to benefit from the advantages brought by the conventional CG, and proposed an Islamic CG that will fit the OECD principles but highlighted some issues of *Shariah* compliance. This suggests that universal standards should be designed to allow some degree of flexibility and still capture the core values of CG. This is similar

to Davies & Schlitzer (2008) in his work showed some highlights on structure of CG, legal frameworks and financial systems as the major causes of the different adjustment or modification of the universal principles of CG of countries and companies. They also pointed out the conception of the “one size fit all” is not suitable for the international design of CG.

Furthermore, trust and honesty are key elements that influences governance framework of any nation or organisation (OECD, 1999). Religious and cultural features of the societies may influence these elements. These characteristics are main practices in the Islamic society such as in Gulf countries where they are perceived as the promoters of Islamic religion (Abu-Tapanjeh, 2009). This could be the reason why the respondents were concerned about their religious and cultural aspect of the conventional CG. As Islam & Hussain (2003) emphasised that in the Gulf countries, the *Shariah* is used as the main starting point of any code of conduct, to reflect on the belief and moral standards that is in line with the cultural and religious features of their countries. These are due to some identifiable differences such as the conventional moral standards with the Islamic moral standards such that every Islamic believer must conform to Islamic law and observe ethical standards derived from Islamic sources *Qur'an* and *Sunnah* (Lewis, 2005).

For example, various principles of good governance and best practices code of conduct had been seen as only to maximise profit, economic efficiency and fair dealings but are also about endeavouring to direct management and control companies to adhere to moral standards acceptable to a society (Gooden, 2001). Despite the best practices of code of CG, it seems to be difficult for the Islamic countries to adopt it because the Western foundation is predominately derived from socially “secular humanist” values rather than deriving it from the religion perspectives (Haniffa & Hudaib, 2006). Again, the Western culture beliefs and values are strongly rooted in self-interest rather than taking wider society interest, even if modified and, finally, in the Western culture the main theoretical framework is based on agency theory rather than stewardship in the case of Islamic corporation in Gulf countries (Davies et al, 1997).

Therefore, from the analysis it was found that the selected Gulf countries could not adopt any conventional code of practice without evaluating it on the Islamic *Shariah* principles and culture. For, cross-border M&A, this may pose serious disagreement between the CG of non-Islamic and the Islamic companies such as the introduction of *Riba* by the Islamic companies based on their fundamental principles (Iqbal & Mirakhor, 2011). For example, the blue chip companies in the West may find it very challenging to start building the CG belief and value to adapt to the Islamic principles. However, they can easily modify their CG code of practice than the Islamic companies that tend to be rigid in their implementation. Also, it is nearly impossible for the Islamic companies to adopt conventional CG without consideration of their Islamic principles and culture.

### **4.3 Corporate Governance Mechanisms**

#### **4.3.1 *Disclosure and Transparency***

This section provides an insight into what kind of information the listed and quoted Islamic companies are likely to disclose to the public in the selected countries' stock market (see question 12 and 17, appendix 3 and 12 and 27, appendix 5). The existing literature suggest that disclosure and transparency are key aspects of CG which need to be implemented to enable successful cross-border M&A with non-Islamic companies. The analysis of interviews of this study showed differences in the degree of implementation across the sectors and the countries. Most respondents from the Saudi Arabia and Kuwait thought that the disclosure and transparency in reporting is higher in banks than in insurance companies and that the enforcement mechanisms was weak. In comparison, firms in UAE experienced better level of disclosure and transparency due to international involvement and this was considered as conducive for cross-border M&A activities. Extant literature emphasise the importance of level of agreement between the two companies relating to the composition of BOD and financial reporting can determine the success or failure of the cross-border M&A on the issues of disclosure and transparency.

It is found that the financial reporting and disclosure of related information is quite similar between conventional and Islamic principles. Abu-Tapanjeh (2009) supported the view by comparing the OECD principle with the Islamic principles, and found that both are compatible in terms of disclosure and transparency. Also, Koldertsova (2011) report on corporate governance frameworks in Middle East and North African suggested that they adopted the OECD principles but were not fully in compliance. However, the study found that it is expected of the Islamic companies to disclose all their financial information to the public based on *Shariah* interpretation but in reality, there is a degree of reluctance, possibly due to some bad practices. For example, one of the respondents from Saudi insurance sector has commented that:

*“Islamic firms are obliged to disclose fairly not only about the financial conditions but also about management of trust money, this goes beyond the disclosure to participation of stakeholders effective control”.* [P5-InsSA]

Also, some of the respondents emphasised that there are degrees of disclosure and transparency among various sectors. For example, some of the respondents reported that the disclosure level of banks in Saudi is higher than the insurance sector, however in case of *Zakat* the (Islamic tax), both sectors had weaknesses. Some of the insurance sector decisions about determining and paying accurate *Zakat*, were not made clear and fully disclosed to the stakeholders. Similarly, there was inadequate compliance of banking sector with the transparency policy, as stated by a respondent:

*“Islamic Banks in SA have much more common with conventional sector, as the CG structure is quite similar; for example, they disclose information regarding debtors and CG to the stakeholders. However, it does not follow the full disclosure policy regarding the ethical*

*responsibilities and achievements of goals relating to the betterment of society. Although they have higher level of disclosure than insurance sector, the features of Islamic banks in SA are not compatible to the spirit of Islamic companies. They disclose very little information about Zakat”.*

[P9-B-SA]

Another expert from Kuwait suggested that the inadequate disclosure could be due to insufficient knowledge within the Islamic banks and this can hinder achievement of the corporate objective of full disclosure and transparency. He said:

*Shariah based organisations have obligation to disclose information on Zakat and transactions involving interest “Riba”; and this can be better done by employing the highly qualified and experienced SSB. [P4-B-KW]*

These suggest that there is no clear code of practice in the selected Gulf countries. This can be linked to bad practices and the reluctance to disclose information. This reluctance could also be linked to culture. Piesse et al. (2012) noted that in Arab countries, their culture refrain them from boasting about their wealth, so both private and listed companies do not wish to publish their financial data and preferred not to comply with disclosure and transparency rules. They also emphasised that despite the requirement in most Arab countries for disclosure of their financial information, most of the companies are reluctant to do so, especially as there was no punishment linked to such violation. Furthermore, it was emphasised by Hassan (2011) that the *Shariah* governance practices in Islamic financial institutions were not fully transparent in their activities and were not granting easy access to the documents of the *Shariah* Boards.

The degree of disclosure could also be linked to the requirements of Islamic principles on the banking sectors, leading to the inclusion of *Zakat* on their balance sheet and the necessity of establishing the Islamic *Shariah* Board, thus adding more structure to the

companies (Alnasser & Muhammed, 2012). Accountability in the Islamic world is two dimensional, one that emphasises corporate accountability to the stakeholders and the other that emphasises individual accountability to Allah, creating dual perspectives, which leads to discrepancies in disclosure (Maali et al., 2006). Furthermore, it is in the Islamic principle for all Muslim to pay *Zakat* as a religious obligation; however, there the requirement for disclosure is unclear (Abdul Rahman & Bukair, 2013). Furthermore, it was suggested that education plays an important role in the level of disclosure and transparency. It was found that the variation in the degree of disclosure was as a result of low education and under-developed conception of CG practices (Haniffa & Cooke, 2002).

Furthermore, the companies in the UAE viewed the disclosure and transparency as very important to carry out the M&A activities. The experts participating in the study viewed the M&A as an instrument to achieve higher level of transparency. For example, one expert from UAE banking sector gave his views:

*“I have observed that banks have cross-border subsidiaries to which they disclose greater level of information because they are in international environment, and this requires them to do so in compliance with regulations”.* [P8-B-UAE]

This shows that Islamic financial institutions do allow disclosure of information to the stakeholder like the conventional ones. Nevertheless, the Islamic financial institutions do not fully comply with the business code of conduct either approved by Islamic or conventional CG. This issue may put hurdles in the way of cross-border M&A as the foreign companies operating in conventional sectors intend to reveal the information to stakeholders regarding every aspect of the company’s operations. Also, since it is required by *Shariah* principles to pay *Zakat*; establish *Shariah* Board and not engage in any conventional practices that require paying or receiving interest, these may hinder the success of cross-border M&A.

#### **4.3.2 Board Size and Characteristics**

This section provides, based on the responses to questions 8, 22, 23, 28 (Appendix 5), provides analysis on the board size and its characteristics. The results show the existence of various Boards' composition and the members that form the various Boards. It also explains how this composition and members of the Board may influence the success of cross-border M&A. It was found that two Boards (SSB and BOD) exist among Islamic companies compared to non-Islamic companies, and it is solely in the hand of the managers to appoint the members of SSB. Also, the BOD in Saudi companies is usually small in size. One of the respondents expressed his view:

*“In a society like SA, we have small size of BOD due to the relationships between families. Many members of the family are serving in the Board or are in the sub-committees of the Board, which is mostly due to the fact that the families own the various companies, and they do not want to disclose much information to the external agents”. [P2-Ins-SA]*

The respondents also stated that the BOD in SA has some weaknesses due to lack of business competencies and experience:

*“The BOD normally comes from family lineage apart from the level of their experience, background and required competencies to run the business. This indicates that members of Board are without the proper qualification, experience, business knowledge and background. It is good to have large Board of directors with mix of experience and qualification”. [P4-B-SA]*

The above accounts are in accord with Hawkamah (2006) finding which reported that in Gulf countries, private companies are preserved by controlling families, which appoint members of the family or friends to serve as independent directors, thus creating room for conflict of interest. Even in the state own companies they include



senior Government officials as Board members which is in line with Al-Hassan et al. (2010), which emphasised that total family ownership is a unique feature of Gulf financial institutions. It is noted that only family member based BOD structure suffers from significant drawbacks arising from possible mismanagement (Saleh et al., 2009), as the composition of the Board would require an acceptable degree of experience and appropriate education, which may affect the decision-making and be detrimental to the cross-border M&A for the Saudi companies. Also resource dependency theory suggests that larger Boards are more likely to pool various experts with diverse industrial experience and educational backgrounds that provide better skills set required by the Boards to have better informed capabilities (Al-Musalli& Ismail, 2012), thus, mitigating individual deficiencies in business skills through their collective decision-making to improve the quality of strategic decision and planning (Abeyseker, 2010).

In the context of the UAE companies, the BOD is much more sophisticated and involved various experienced members. The members of their BOD come from various background and foreign nationalities. This means that they can provide more experience and knowledge for performing cross-border M&A effectively. This view is similar to Weir et al. (2002), noted that the Board size and composition have an influence on the firm and its financial performance. This is in line with Abeyseker (2010) comment above. For example, the view of one of the respondents in the context of composition of BOD:

*“The UAE has a more open environment in contrast to SA, which is more conservative. The composition of the BOD involves foreign experts, women, educated and experienced members in order to make sure that BOD is rich with various people who can contribute positively towards expanding the boundaries of the business”. [P6-B-UAE]*

This indicates that BOD in companies from the UAE also involves women, which are rare in Saudi environment. This also indicates how flexible and open BOD composition and has better integration with various ethnic backgrounds. Furthermore, they can have

a beneficial mixture and gain from their experiences, which can provide the edge for expansion and making the deals with foreign companies in insurance and banking sector. In addition, the BOD reveals a greater deal of information to the external parties' relating their responsibilities towards the shareholders of the company, which can be a contributor to make the cross-border M&A effectively compared to the Saudi companies. The participants viewed that open environment in the Gulf countries can overall increase the efficiencies of the local companies to fulfil their ambitions of business expansion. One of the respondents from Kuwait was of the view that:

*“BOD members in Kuwait are not independent and are influenced by the management or a controlling shareholder. Most of them are qualified and experts to work in Kuwait or within the Gulf region, however, they are yet to be efficient enough to cross-border”.* [P8-Ins-KW]

The Board size and family ownership likely affect the ability for the Board members to control and influence all transaction of the Islamic financial institution and to ensure their operations are in compliance with the rules and principles of *Shariah*. However it may be a concern for cross-border M&A from non-Islamic companies in terms of the controlling structure and may generate conflict of interest.

In summary, the analysis of the empirical data showed the existence of dual BOD structure (SSB and BOD) in Islamic companies and that company managers have a great latitude in appointing the SSB. In addition, the majority of the respondent perceived the difference in composition and the functioning of the two boards between Saudi Arabia and Kuwait, and UAE. They analysis showed that family control and family membership, without having relevant business competence and experience, dominate the structure of the boards in SA and Kuwait whilst boards in the UAE tend to be of a large size and constitute diverse board members with appropriate experience, knowledge. In latter, case women also are represented in the Board which is a rare phenomenon. This analysis in part addressed the research question relating to the CG mechanism in this study context.

### 4.2.3 Ensuring Compliance and Transparency

This section, explores the roles played by the independent external auditor on how they contribute or influence the financial reporting process of Islamic companies, and how this influence cross-border M&A. The analysis in this section is heavily drawn from the responses to interview questions 7 and 15 (Appendix 4 and question 16 (Appendix 5).

Most of the previous literature has not assessed and identified the key role the external auditors play in the Gulf countries. However, the work of Safieddine (2009) emphasised that the independence of external auditors play an important role in the disclosure and transparency of financial reporting and it is associated with the decrease in financial fraud. This study found that there are two different types of independent external auditors (*Shariah* external auditor and conventional external auditor). UAE has both but the *Shariah* independent external auditor does not exist in SA and Kuwait and this has a negative impact in term of level of disclosure and transparency. Even in case of UAE, the involvement of the independent *Shariah* external auditors is quite recent and the evolution of practice is still to achieve a standard comparable to Malaysia. In SA and Kuwait there are shortcomings identified in the conventional external auditing, such as:

*“Poor communication between the audit committee and external auditors, moreover, the external auditors are constrained in reporting independently and they have to do so in conjunction with internal auditors”. [P7-B-SA]*

This highlights a potential conflict of interest between the external and the internal auditors in terms of decision-making process, especially in how *Zakat* is calculated so that the company can get away by paying a lower amount of *Zakat*. It also indicates that the internal auditors may be influenced by management in terms of procedures and principles of best practices and in turn they influence the external auditors. The problem, in many cases, arises from inadequately trained and professionally well qualified internal auditors. This has been observed by Al-Shammari et al. (2008), who noted that no company among the Gulf countries achieved full compliance with the international accounting standards or disclosure requirement due to lack of professional

training and unattractive salary for most qualified people, and lack of appropriate compliance standards for Islamic companies.

Baydoun et al. (2012) further noted that in Gulf countries, external auditors are ineffective because they are poorly informed on companies' matters as companies will say one thing and do another thing. Hussain et al. (2002) emphasised that in Gulf countries, some practices do not match with their social-cultural and religion norms in respect of the Islamic financial accounting best practices. The situation is further compounded by lack of confidence in terms of practices by the conventional external audit and lack of competition as reported by one respondent:

*“In my view, problem we are facing in SA is that there is a lack of confidence in the performance of Saudi Audit firms. In addition, the monopoly of audit services by some audit firms is another issue affecting the performance of external auditors”.* [P8-B-SA]

Similar views were expressed by the Kuwaiti respondents from banking sector, as exemplified by one expert:

*“Many Shariah Board members and Shariah auditors are not involved in financial details, as they believe that they don't contradict Shariah guidelines. This is mainly because of lack of financial, accounting and economic background. There are no independent Shariah external auditors involved in the financial reporting”.* [P6-B-KW]

However, the banking and insurance sectors in the UAE are more organised in terms of functioning and independence of external auditors. One expert from the banking sector in the UAE reported:

*“In the UAE we have the qualified and experienced external auditors and rotate them regularly to ensure the required level of disclosure and transparency in reporting system. We are in the process of improving our decisions relating to the selection of the most appropriate external auditors based on the international criteria to attract the investors”.*

[P9B-UAE]

This highlights the higher level of alignment of Islamic business principles with the international standards of CG, which gives the Islamic banks and insurance companies a better chance to make cross-border M&A with the foreign companies.

The preceding discussion highlights the need for external *Shariah* audit to ensure better compliance with *Shariah* principles and along with the conventional external audit, provide a harmonisation of *Shariah* principles with the international standards of CG. There is need for continuous improvement in implementation of CG in Gulf countries to create more favourable business opportunities for merging with and acquiring non-Islamic companies (Othman & Ameer, 2015). Al-Shammari et al. (2008) noted that improvement in international accounting standards in the Gulf region will facilitate the process of attracting international investors.

This study found the existence of two different types of independent external auditors (*Shariah* external auditor and conventional external auditor) but these do not appear to be uniform across the countries. The analysis of the interviews suggested that many respondents thought that UAE performs better in having both kinds of independent external auditors but less so in both the Saudi Arabia and Kuwait and these would have negative influence when seeking cross-border M&A between Islamic and non-Islamic companies. Factors such as inadequate professional training, less availability of qualified auditors, lack of organisational incentives for qualified personnel and lack of appropriate compliance standards for Islamic companies explain the less robustness of *Shariah* compliance mechanism in these countries. The three issues (disclosure and transparency,

board size, and compliance with the *Shariah*) discussed in this section addressed the research objective relating to the CG mechanism and the extent to which firms comply with the CG *Shariah* principles.

#### **4.4 Incorporating Islamic Principles (Shariah law) in the Business**

##### **4.4.1 A scope of International M&A**

The finding of this sub-theme is based on the responses to (question 9, appendix 3), (questions 18 and 19, appendix 5). An overwhelming majority of the respondents believed that implementation of *Shariah* informed code of practices does not constrain on the cross-border M&A if the salient values of *Shariah* principles such as fairness, social responsibility, honest and promoting ethical businesses are observed. Further, some interviewees noted the fact Islamic finance has become a significant player and integrated into the international financial system and hence provided scope for M&A activities globally. According to one senior manager, adopting *Shariah* law code does not limit the scope of business only to Muslim countries, as one of the respondents has said:

*“Islamic principles of business do not prevent the expansion of business beyond the local boundaries. Islam has begun to spread in non-Islamic countries; therefore, we have customers outside the country, to which we serve the products and services which may not be available in their countries”. [P16-Ins-SA]*

The above view explains the reason why Islamic companies can be found engaging in business with various non-Islamic companies in different countries such as UK or US. Similarly, Abu-Tapanjeh (2009) noted that Islamic principles practiced by Islamic companies encourage expansion of businesses in a fair and honest manner. Both the Islamic and non-Islamic companies have similar view on social responsibility, and they both make use of various means to screen unethical practices of companies (Ahmed, 2010). For example, both Islamic and non-Islamic companies do not promote any prohibited goods and services depending on their value systems. Islamic financial

institutions in Gulf countries have demonstrated willingness to expand their services to non-Islamic companies as long as they are prepared to adjust to their fundamental principles such as *Riba*. Islamic companies have potential to grow, to integrate with or have a corresponding memorandum of understanding with non-Islamic companies who are looking to invest ethically and adjust to the underpinning of Islamic financial practices (Temperal, 2011).

Furthermore, the international perspective of Islamic finance assumes significant relevance as it increasingly becomes integrated with the international financial systems, thus forming a financial network chain of intermediaries and provides platform for market expansion in various regions, contributing to a better financial resource allocation (Kammer et al., 2015). However, there are essential issues that need to be resolved in order to promote and encourage business expansion, which includes concerns on how to adapt or resolve economic policies differences and the formation of trustworthy policies between states and transnational corporations (Sole, 2007; Dakhilallah & Miniaoui, 2011).

Therefore, it is important to find ways to enable both the Islamic and non-Islamic companies to coexist for the purpose of increasing economic activities and human development in more acceptable ways. The foreign companies that deal with companies from Islamic countries are deemed to deal with them "in a special way", to accommodate the complexities involved in applying the *Shariah* governance code.

#### ***4.4.2 Shariah Screening of Products, Services and Transactions***

The findings in this sub-section attempt to answer the research question relating to what extent *Shariah* law and associated principles are used in business practice and how they encouraged the cross-border M&A between the Islamic financial companies from the Gulf region and non-Islamic companies from the West. Responses to interview questions 13, 14, 18, 19 & 29 provided evidence on this issue (appendix 5) and questions 11, 13 and 16 (appendix 4). Many respondents agreed in their views that incorporating *Shariah* principles restricts the extent to which Islamic financial companies engage in cross-border M&A with non-Islamic companies. They identified

factors such the prevalence of interest charging practices, complexity of Islamic mode of financing and risk management as well as limited number of Islamic financial instruments to limit the scope for M&A. In addition, they argued that the monitoring of regulatory authorities in these countries to ensure the compliance with *Shariah* law and principles and the lack of interest by *Shariah* scholars also negatively affect the cross-border M&A issues. In contrast, some respondents made clear the fact that the bulk of M&A deals in the Islamic world are funded by conventional acquisition finance.

It was found that there are regulatory bodies that try to assess and identify transactions, services and products or practices that are not *Shariah* compliance driven. One of the respondents in SA stated that company is committed to the Islamic principles, regardless of where it makes the deal for cross-border M&A:

*“The company is committed to the application of Islamic law in all its dealings, even in its dealings outside the country. All of the company’s investments are monitored by the Monetary Authority and all of its contracts must be compliant with Islamic law. The international companies begin to understand our need to apply the Islamic law, thus they deal with the Islamic companies in a special way to allow compliance with Shariah, and we always stay away from Shariah warnings such as interest”.* [P12-Ins-SA]

Another respondent in UAE has expressed similar view:

*“This is not a hindrance because the investments in the permissible areas are many and profitable, and choices are available for Muslims and non-Muslims. I think that the Gulf investors succeeded in large projects recently, which are permissible investments”.* [P7-B-UAE]



This shows that there are regulatory authorities, which oversee the investments of the companies in the foreign countries and pass their verdict on the legitimacy of such transactions in the context of Islamic CG. This implies that transactions or practices of the companies regarding the cross-border M&A may affect the M&A activities if any agreement is found to be against the Islamic CG. However, if the M&A are mediated with Islamic companies in the non-Islamic countries, then there would be no effect on the M&A, as both participating companies in the transaction follow the same or similar Islamic business principles. However, the companies may also be monitored by the ministry of commerce (Hassan, 2010).

In contrast to the Islamic companies adhering to *Shariah* compliance, IFR report (2009) on Islamic finance and the M&A gap noted that the vast majority of M&A deals in the Islamic world are funded using conventional acquisition finance. This suggests that there are no global-compliant frameworks in place for Islamic finance and this hinders the growth of Islamic financial products. Islamic CG practices may prevent the spread of local Islamic companies to cross-border M&A, as they face many challenges in the non-Islamic world. Respondents from the banking sector have expressed these views:

*“Yes, we participated in M&A, and Shariah law does not encourage practicing these deals and this is a barrier that hinders working abroad because there are many issues we avoid practicing since they are contradicting Islam such as the Riba”.* [P3-B-KW]

*“Following the Shariah law restricts our business due to the limitation of Islamic investments imposed by the level of compliance of Islamic principles by the host companies”.* [P10-B-SA]

However, some of the respondents from the banking sector raised an interesting point during the interview that the Islamic values affect the M&A activities, but the *Shariah*

scholars are not really interested in understanding the activities of non-Islamic countries or companies, though they always have the power to over any decision of M&A. Also the *Shariah* scholars are not interested in creating a means to improve or innovate on Islamic products or instruments for non-Islamic companies to support economic activities and human development.

#### **4.3.3 Legislative Provisions**

Legislative provision formed one of the sub-themes of incorporating Islamic principles. From the interview analysis (based on the interview questions 5, 8, & 16, Appendix 3), it was found that in all the three countries, there is no clear well-defined legislation on how Islamic companies engage in M&A locally or at overseas locations. Though companies could use statutory laws to do business, they need to comply with the Islamic principles which are subject to *Shariah* Scholars' interpretations which at times vary from scholar to scholars. The subjective interpretation, lack of formal legal provisions and the consequential attitude and behaviour of senior managers pose major challenges in the motivation and process of cross-border M&A. The ways in which *Shariah* scholars to interpret *Qur'anic* text and *Hadith* is crucial in determining the motivation for companies to merge internally or in other countries. This said however, the extent which legal provision is said developed and used as well as their influence on international M&A varied between the countries .

This section discusses the mechanism that the Islamic company follows to do business with non-Islamic to formalise a deal on cross-border M&A. It was found that in all the three countries, there is no clear well-defined legislation on how Islamic companies can expand or formulate formal agreement to conduct any business interactions with a non-Islamic company. As one of the respondents said:

*“There is no Islamic legislation written for the businesses, which can offer some legislative obstacle for M&A deals. The expansion of the business is always promoted by the statutory laws of the state. The statutory laws state that Islamic companies within the Muslim country cannot do business without implementation of the Islamic principles, but there is no*

*law regulating the international M&A of companies in the non-Islamic world, which has often failed the deals”. [P7-B-KW]*

The lack of legislation may be attributed to a passive approach in (SA) which prefers to self-initiative rather than regulator’s direction, or minimalist (UAE) approach, which prefers the market to develop its own *Shariah* governance system rather than a greater intervention on the part of regulators (Hassan, 2010). However, the above view suggested that the absence of clear rules and regulations may hinder the transparency of conducting business. This can serve as a barrier for the companies in making international M&A deals. This account is similar to Lewis (2005), which affirmed that rules and regulations of Islamic CG need to be organised, clear and unified. The lack of law causes confusion among the company BOD about what approach they need to adopt to make cross-border M&A deals and such confusion can lead to subsequent failures. Lakshamanan (2014), in his article on risk management in Islamic banking in relation to mergers and acquisitions, also suggested that there is a need for regulation in order to ensure the success of M&A as there is risk embedded throughout pre and post deals stages.

However, Hassan (2010) stated that article 2 of the constitution of Kuwait vividly put *Shariah* as a main source of legislation and Islam as the official religion and in spite of the minimalist approach they expect the Islamic financial institutions to have proper *Shariah* governance system. However, the conventional business has no such restraints. One of the respondents from the banking sector of Kuwait expressed this view like:

*“If expansion is inside the Islamic states, it will not affect the M&A deals, however, the international M&A deals outside the country with companies in non-Muslim world can face some obstacles from Islamic regulatory institutions and many other local authorities in Kuwait, for example observing the code of conduct of Islamic companies outside Kuwait. If we do anything against Islamic principles outside the country, then it risks the company reputation within the country, therefore, we have not as many*

*opportunities of making international M&A as the conventional banking sector does”*. [P6-B-KW]

From the above comments, it seems that Kuwaiti banking sector is more cautious about making cross-border M&A deals due to possibilities of subsequent challenges by the regulatory authorities. Also, there is a similar view in UAE. A respondent from the UAE banking sector:

*“The problem does not arise from the implementation of the Islamic principles and way of doing business; it mainly comes from the rigid and strict thinking of scholars and policy makers. There are several business opportunities such as merger of Islamic banks with non-Islamic banks that are willing to merge for providing the financial service to Muslim minorities in the European countries. So we need to think about these issues seriously”*. [P3-B-UAE]

This indicates that the problem heavily lies with the *Shariah* supervisory Board and not with the *Shariah* principles. This is similar to Choudhury &Hoque (2004), which affirmed that Islam allows the *Shariah* scholars to interpret *Qur’anic* text and *Hadith*, thus leading to confusion and misunderstanding of the principles of *Shariah* either by the Muslim or non-Muslim such that the extremist interpret it to suit their own agenda while the moderate would offer different interpretation. Although the Islamic principles may have some base-line restrictions in business dealings, the possibility of moderate interpretation offers opportunity for the expansion of business. This is similar to one of the respondents from the insurance sector of the UAE views:

*“There is an Islamic economic jurisprudence which can provide a lot of guidelines in terms of guiding the path to make transactions within certain boundaries and flexibility by being in the Islamic domain, such as financial and economic transactions based on estimated way of being Islamic if the guidelines are not clear in their own right. The M&A*

*between Islamic and non-Islamic companies are always judged in the context of the Islamic jurisprudence which can provide more flexibility to business in the matter of business involving certain degree of obscurity”.*  
[P11-Ins-UAE]

This shows that insurance sector is more optimistic of the innovative aspect of Islamic principles and their ability to deal with new issues from emerging business opportunities and technological advances. M&A can be improved, based on the above views, by taking into consideration the effective management of economic aspects of Islamic principles.

## **4.5 Cultural Influences**

The existing literatures suggest variations in culture from country to country would result in different business policies, leadership styles and management practices of the companies (Licht et al., 2005), and these are likely to affect the decisions about the international M&A. The interview analysis (based on the interview questions 19 (appendix 3), question 25 (appendix 4), and question 31 (Appendix 5) generated three sub-themes: Islamic inheritance, women at workplace and business culture and decision making and these are discussed below.

### **4.5.1 Islamic Inheritance Law**

This sub-theme examines the extent to which the differences in culture across Gulf countries influence the decision regarding cross-border M&A. In doing so, it attempts to address the research question relating to what cultural factors facilitate or constrain cross-border M&A. This study found, based on the all respondents' account, that in the context of the three countries issues relating to Islamic inheritance have a strong influence on decision-making regarding cross-border M&A and its influence is likely to be more of constraining than enabling. Based on Islamic principle of inheritance, as a social value and custom embedded in the *Shariah*, the values of the business is transferrable to the closest blood relative of the business owner. Such practice is always considered first before anything that has to do with the business. Two respondents from

the banking sector in SA, for example, reported that a variation in culture causes different issues that influence their decision on certain matters:

*“In our social values and customs, the families own the businesses; the management of the companies is taken over by the relatives and sons of the main owners. In other words, businesses are transferred to the next owner based on the law of Islamic inheritance”. [P17-B-SA]*

*According to Islamic law of inheritance, the ownership of business is transferred to the closest blood relatives of the owner, when it comes to the selection of members of Board; the priority is given to the relations and friends of the owner, which can decrease the possibility of M&A especially if they are inexperienced and non-qualified. [P3-B-SA]*

The above comment suggests that there could be a lack of clarity for non-Muslims on the procedure of transferring business ownership. Adhering to *Shariah* suggests that in dealing with cross-border M&A such practices have to be clearly stated and embedded into any agreement. Stahl & Voigt (2008) emphasised that the cultural differences across countries, including organisational cultures, affect socio-cultural integration, synergy realisation and achieving shareholder values in different ways. Such transfer of the business to any blood relative may have some implications in respect to best practices on CG, if the person that inherits the business is not competent or knowledgeable to carry on with the business management.

Zollo & Singh (2004) noted that striking the right balance between the acceptable levels of organisational integration and mitigating the level of disruptions of the acquired firm resources and competences is a strong challenge in terms of M&A. The family ownership suggests that it can be more efficient on running the business for both the family and shareholders. Khanna & Palepu (2000) emphasised that in term of asymmetric information the transaction cost among family structure of business and

close corporate affiliate is lower compare to other structure. However, clear understanding of the owner's family structure is a strong challenge in respect to cross-border M&A. The qualification and merit of the employment are the secondary considerations, which can be problematic. A respondent from insurance sector in Kuwait expressed the view:

*“In Kuwait we witnessed several issues regarding the selection of members of Board based on the criteria of how strongly the candidates are related to the owners of the firms. In Gulf countries, we still have long way to go to select a competent BOD for making the absolute and non-partial decisions of the expansion of business within local market and international arena”. [P8-Ins-KW]*

These comments shed light on the overall practices of firms in Gulf countries in general and of Kuwait insurance companies in specific, regarding the appointment of BOD. Stronger BOD can play an important role in making the decisions of M&A with minimal risk to the integrity of business. This is similar to the work of Sabi (2015), which affirmed that lack of organisational structure, legal structure, and effective CG structure of family business in Gulf countries are strong barriers for smooth transition, as they practice conservative management style rather than innovative management style.

However, in the UAE, the situation is much better than SA and Kuwait. They take more liberal approach towards the management of the firm. The respondents from the insurance sector of the UAE commented:

*“The companies in the UAE value the merit, experience and qualification of the candidates applying for the posts of the managerial positions, rather than giving priority to the blood relations or friends of the owners of the companies. I am in favour of such policies because it prevents the*

*management from taking immature decisions regarding M&A and putting the business at great risk”. [P4-Ins-UAE]*

The above comment still shows the practice of family style of ownership and management. Despite being more flexible, the family style of running a business is not efficient and breadth of knowledge and experience when it comes to cross-border M&A. Braun & Sharma (2007) emphasised that the family ownership of business suffer drastically from agency problems and severe managerial entrenchment. Also the work of Safieddine (2009) emphasised that in any business there is issue of conflict of interest between the strong shareholders and weak shareholders and stated that for greater control over the business a greater concentration of shareholding is required. Therefore, the proportion of family own businesses in Gulf countries is very high, which creates a strong cultural barrier when it comes to cross-border M&A as this will entail complete restructuring of the whole business, compromises to ensure compliance with the legal framework and have a well-defined memorandum of understanding.

#### ***4.5.2 Women at Workplace***

This section explains the main challenges of women to be represented in the BOD and work in mixed workplace in the selected Gulf countries and how these can affect or influence cross-border M&A. It was found that there are variations among Gulf countries in woman participation in the management and in BOD. For example, in SA, from the insurance and banking sectors it was found that mixed workplace is not allowed and that women are only allowed to work in places where there are only women, while in UAE and Kuwait mixed workplace is allowed so women are allowed to work with men in the same environment. This is comparable to the European companies, which value the diversity at workplace including equal rights for men and women at workplace. The lack of working rights to women in insurance companies and banks in SA can be an obstacle in dealing with non-Islamic companies across international M&A. This point has been raised by some of the respondents from the insurance sector in SA.



*“Yes, there are cultural barriers to women working in the mixed environment. Due to variations in the cultural environment between the two merging companies, this factor can be one of the main causes of the failure of M&A deals. This is not religious, but a cultural constraint. For example, Prophet Muhammad (s.a.a.w) allowed women to work side by side with men during periods of war and enjoyed similar status in other fields like business ownership”. [P12-Ins-SA]*

However, another respondent from the insurance sector commented on the changing nature of culture:

*“The Saudi Government adopted the policy of sending the Saudi nationals to foreign countries to get assimilated with the foreign culture; this will make them open-minded and increase their tolerance level toward accepting women at work places”. [P1-Ins-SA]*

The above comments do highlight the fact that Government in SA is willing to change its stance for women to work in workplace with men. However, it is not clear when such instance will come into law or pass legislation for allowing women to work in a mixed environment. Recently, the Government have started introducing some initiative to educate their people on the right to allow women to work in a mixed environment. First, providing educational platform to provide exposure to the younger generation, especially students, to foreign world and this will automatically have positive influence on the attitude of the young generation. However, not having a clear policy yet is still a dilemma for women in Saudi Islamic companies. As it is clear that there are regulation that does not allow mixed work places, for example Alhabdan (2015, p.3) stated that “Saudi Labour Code indicates that an employee has to comply with the provision of Islamic *Shariah* which has been understood to prevent gender mixing ...the Labour Force Counsel issued Decree number 111/8 to illustrate the conditions for women working. The decree states that “for women to work, a woman must first obtain permission from her guardian, the work has to be appropriate to her nature, the work

must not have any risk of physical or social damage, and finally, a woman must be separated from men in the workplace” .Also Al-Ahmadi (2011) emphasised that even when women work in the same place with their fellow women, they are faced with many challenges that hinder them from being an effective leader due to lack of resources and lack of empowerment.

In contrast, to rigidity and conservative practices of SA for not permitting women to work in mixed environment, both Kuwait and the UAE have more liberal stance. Some of the respondents from the banking sector in the UAE stated, for example:

*“The Emirati women are more liberal and Government policies are more oriented to the exposure of the women in the UAE to a variety of the business culture, allow them to work in mixed environment so that they can learn better organisational skills by working side by side with men at work places. The companies send the women along with men as delegates to foreign conferences to meet the leadership of foreign companies. This makes them better prepared for any cultural change in future through international M&A deals”*. [P1-B-UAE]

Also in Kuwait, some of the respondents stated that:

*“Women in Kuwait want to serve in insurance sector and they are seen as being socially better adept at making good contacts and they are good planners and managers. The success of the business is ensured in Kuwait by giving equal opportunity to men and women at work places. They can rise to the position of power and influence. The formal law regarding protection of women from harassment at workplaces are designed in Kuwait”*. [P2-Ins-KW]

*“The banks management are more careful in recruiting women for managerial positions due to stranger attitude of men toward women at workplaces. By law, it is not prohibited to allow women to work with men, but the management is more interested to keep the working environment free of any troubles”. [P10-B-KW]*

These comments show that both Kuwait and UAE allow women to work in mixed workplaces, but there are still some cultural barriers. Broadly, they perceive women as an important aspect of CG and view their contribution as significant to the success of their company. Such analysis ties in with the observation of Al-Yousef (2009) in that the status of women in Gulf countries varies but has evolved significantly to the scale where their contribution to achieving organisational goals being recognised. Hawkamah (2013) also emphasised that the Gulf countries are shifting towards providing women with market oriented education to increase the women labour force as they are seen to be more in touch with staff, customers and stakeholders. Women also characterised by their transformational leadership style and better team spirit as well as a greater diversity leading to better decision making as men and women might interpret their experiences differently and bring alternative perspectives, which are a significant contribution of the multi-cultural workforce (Omair, 2010). Despite the banking sector in Kuwait being more cautious in recruiting women as discussed earlier, this is not the legal position and women are encouraged to work with men and the selection process is free of prejudice.

Though there are variations in women working in various Gulf countries, even in SA that does not allow mixed workplace, there is a beginning of realisation that women too can contribute in managing organisations and that they feel optimistic future changes towards a mixed workplace. This observation on the ground aligns with Ellis et al.'s (2015) finding that 85% of the women in the Gulf countries want to take up leadership role in a mixed work place.

#### **4.5.3 Business Culture and Decision-Making**

This section reports on the respondents' views on how business culture and decision-making process affect the cross-border M&A in particular when applying Islamic principle of CG to non-Islamic companies in non-Islamic countries. It was found that there are different approaches to business dealings between Islamic companies and non-Islamic companies, which could be attributed to differences in culture. The respondents from the banking sector were of the view that Western companies have different approach in terms of setting up and running a business. Firms in Western countries context can take up interest payable loans to expand their businesses, while in Islamic companies, the loan with interest is considered unethical and hence prohibited. This may limit the capability of investors to expand their businesses through M&A activities. The investors in SA have no investment culture; they have only financial resources pooled up from their relations and families. These financial resources are normally derived from trust based and interest free loans. However, there may be less limitation on how much they are willing to provide compared to a financial institution that will base their decision on the capability of the business to repay such loan. These practices may have a negative impact on cross-border M&A. For example, one of the respondents from SA said:

*“There is no investment culture in SA in the stock companies. There is more speculation and uncertainty in the business environment of Saudi due to weak understanding of the investors about the business opportunities. The local investors do not take the long-term investment opportunities”.* [P12-B-SA]

The above comment suggests that this lack of investment culture may be caused by their cultural belief and values, which create the differences between the Western and the Islamic culture. This view is similar to Stulz & Williamso (2003), which affirmed that the business practices vary with culture; the people have different approach to the business based on their regional customs, norms and values. David & Singh (1994) noted that cultural differences are one of the key challenges that represent the source of acquisition cultural risk, which has a potential obstacle for achieving integration

benefits. This is also consistent with cultural distance hypothesis which suggests that cost, risk and difficulties associated with cross cultural contact increases with cultural variations among organisation, groups and individuals (Hofstede, 1980). Also, work has been carried out to strike the balance as a result of the variation of culture but emphasises have been in achieving the necessary level of how to minimise any disruption and bolster integration with available resources and competencies is the fundamental challenge that affects the success of cross-border M&A deals (Zollo & Singh, 2004). The “poor understanding” and lack of “investment culture” may be the key challenges that may affect the capability of Saudi companies to participate in cross-border M&A activities. However, the insurance companies in SA are more optimistic to engage with foreign companies. The insurance companies are more dependent on the foreign insurance companies for the stabilisation of their business. For example, one of the respondents from the insurance companies said:

*“The investors in insurance sector are likely to engage in real entrepreneurship when it comes to collaboration with foreign companies. After all, conglomerations run the insurance business in insurance sector. Investors cannot expect the higher share of profits without taking risks”.* [P16-Ins-SA]

This indicates that the culture and values may still be influenced by the interest in the nature of the business that the investors want to engage. Therefore, insurance sector is more likely to invest outside SA, deal with foreign companies and enter into the M&A deals with them, as the investors are willing to take risks.

Furthermore, there are indications that the Arab nation are always show sign of unwillingness to implement new strategies and unwillingness to work through challenges in forming new companies (Deloitte, 2009). For example, respondents from both banking sector and the insurance sector also emphasised that lack of understanding of the business concepts used by Western country companies and vice versa may

influence their decision making capability. Kuwaiti insurance and banking sector respondents said:

*“Applying home CG to other countries is difficult and it is seriously hindered by the lack of negotiation process, which mainly stems from the lack of understanding of behaviour of people, set of beliefs, interactions and relationships and timeliness of the business operations. These factors can reduce the possibility of M&A deals between the Western-based companies and Islamic companies”.* [P8-Ins-KW, P6-B-KW]

The above expressions indicate that cultural differences between the Western and Islamic world may give rise to many problems and issues which may affect their decision-making processes. The factors, which are important for the West, may not be important for the Arab point of view. For instance, time is very critically important in daily life of European people, while in Arabic world is always taken for granted. Also Arabic lawyers only have much knowledge of the legal system in Arabic countries based on *Shariah* principle and they don't have better understanding of the Western legal system, which may slow the decision making process. This view is supported by Deloitte (2009) that different decision-making styles can lead to slow decision-making and it may lead to failure to implement decisions. These differences in cultural traditions and norms may affect cross-border M&A deals.

Finally, the culture of Islamic world is perceived as a threat to the Western world and businesses, which make the expansion of Islamic businesses difficult. One of the respondents from banking sector expressed his view that:

*“Some business communities outside the Arab world consider Arab culture and people as a threat to their stability, especially after 9/11 attacks. Media played a role in distorting the image of Arabs and Muslims as whole by labelling them terrorists. These conditions make the cross-border expansion almost difficult for banking sector in the UAE”.* [P4-BUAE]

This view demonstrates that the factors, which can prevent the expansion of business into the Western world, include the perverted view in the host community, about Muslims and Islam, makes the expansion more difficult for some businesses. This is consistent with Islamic threat perception which emphasises that Islamic revivalism has often been seen and experienced as direct threat to liberal beliefs, interests of elite secular ideas as well as multinational corporations and Western Governments (Esposito, 1999). Also, in recent years, the social, political, global and regional developments have affected the relationship between the Islamic countries and Western countries throughout the world. People are witnessing an evolution in the perception of Islamic religion based on the notion of terror activities and violence faced by Islamic and non-Islamic countries especially from people pretending to act “in the name of Islam” thus leading to increase in prejudice and misunderstanding of both sides (Mesic, 2004).

Therefore, from the comments and the discussion, it has shown there are variations of culture between the Islamic and non-Islamic countries companies, which may slow decision-making process. Also, this discussion has shown that there is an increasing tension between the non-Islamic and Islamic countries due to the terror activities and violence, which may affect cross-border M&A dealing.

In summary, the interview analyses provided evidence which suggests cultural differences between the West and the Muslim countries influence the ways in which businesses get managed and decision is made. The data showed under developed business acumen and lack of investment culture, difference in decision making style and the recent unhealthy perception about the Islamic religion combined would likely to hamper the cross-border M&A activities between Islamic and non-Islamic financial companies. Sector-wise, the study found that the insurance companies are more likely to engage with foreign companies than banks due to their heavy reliance on foreign firms for stability and likely to invest overseas.

## 4.6 Need for Shariah Compliance

### 4.6.1 Effect of Shariah Scholars' Interpretations

The presentation in this section addresses the research question and objectives relating to the influence of *Shariah* principles interpretation and compliance in view of cross-border M&A with non-Islamic companies. The analysis heavily relied on the responses provided by respondents to interview questions 7 and 18 (appendix 4) and 20 & 25 (appendix 5). It was found that the M&A activities involved greater complexity due to differing interpretation of *Shariah* by Islamic scholars based on their liberal or conservative outlook and understanding of business issues. This can be a major factor, which can either restrict or promote the cross-border M&A with non-Islamic companies in the Western countries.

The analysis of the many respondents indicated that companies in these three countries had to make subtle, delicate, business dealings: simultaneously managing the competing view of meeting customers' needs with complying with the *Shariah*-based business principles. The task becomes much more difficult and onerous given potentially conflicting interpretation of *Shariah* law and principles by *Shariah* scholars when these being applied to businesses as cross-border M&A involves complex processes and outcomes. In nutshell, the more conservative the *Shariah* scholars' interpretations of the *Shariah* principles, according to the respondent's analyses, the more difficult it would be to undertake effective cross-border M&A. The monopolisation of the market by a few *Shariah* scholars is likely to lead to principal and agency problem due to the conflict of interest.

One of the respondents from the insurance sector has reported that anything, which is seen as going against *Shariah* (for example dealing with undefined or uncertainty), can prevent the business deals with other companies:

*"A customer came to us and wanted us to insure the big tower he built in the city. His deal was to insure the tower building against any kind of danger or hazards. This meant that in the event of any disaster, the*



*insurance company is required to pay off all the damage to the tower and this is unlawful in the sight of God. This was against the Shariah principle as it is kind of playing with chances and it is considered as gambling by Shariah scholars, so we didn't accept such insurance proposal". [P15-BSA]*

This showed that Islamic insurance business in SA is heavily subject to *Shariah* interpretations and insurance companies which are conservative in interpreting the Islamic principles will find it very difficult to carry out any M&A with a conventional insurance company. This is similar to Khalid (2013), who noted that different Gulf companies have different *Takaful* (Islamic insurance) guidelines and rules which create difficulties in any M&A and emphasised that the task can take longer to negotiate, structure and execute. Such practices also create difficulty in developing a uniform regulatory framework across the Gulf region. Hassan, (2011) carried out a survey on *Shariah* governance practices, which found that there were diverse *Shariah* governance practices among Gulf countries, leading to shortcomings and weaknesses and there is need for uniform regulatory framework.

Also the society is widely aware of the *Shariah* principles and adheres to it, frequently acting as a watchdog in Gulf countries and insisting on *Shariah* compliant products. For example, one of the respondents from Saudi insurance company corroborated this:

*"We exclude everything that opposes Shariah, because our first goal is to satisfy the customers, almost all of whom adhere to Shariah and search for products that are in compliance with the Shariah principles. The success of the insurance company depends on the customer satisfaction and obviously we are working within an Islamic environment". [P13-Ins-SA]*

The above comment shows that the general principles of business are applied but once there is a contradiction or variance with the principles of Islam, such practice will not be used. This applies to even globally accepted ways of doing business. This is similar to Chapra & Ahmed (2002), who noted that large percentage of

capital providers, shareholders and investors to Islamic financial institutions are very concerned that their stake is fully in compliance with the *Shariah*.

Agency problems arise in conventional companies when managers deviate from their task and responsibility to maximise shareholders wealth and their own return. In Islamic companies, there may be further agency problems arising from those who oversee the *Shariah* compliance (Safieddine, 2009). One respondent said that:

*“Shariah scholars who have monopolized the market serve on multiple SSB and earn fees may lead to rigorous challenge. This may raise a conflict of interest and affect confidentiality of the business. There may be risk of leaking of information that can impact the competition in the market and the development of Islamic finance ...However, some Shariah scholars search for clever ways to circumvent some fundamental principles, which leads to the disappearance of any credibility to applying Shariah in companies”.*[P5-Ins-UAE]

Such agency problem arises from the flexibility allowed by Islam to take cognisance of the context within which an appropriate principle can be applied, provided it does not violate the clearly stated prohibitions. One respondent commented on that:

*“Different interpretations of Shariah are considered as a kind of flexibility and mercy in Islam. The non-Muslims think that this is a disagreement on the Qur'an because they don't understand that this is called Jurisprudence according to the circumstance. Difference is normal and this exists in Shariah. And if there is no difference, we would doubt the actions as extracting the law differs from one member to another. However, we get worried about the difference in the fundamental Islamic principles, in its case and there is no way to argue about it”.* [P15-B-SA]

Though it would be permissible in terms of *Shariah*, effect of these variations needs to be examined in the context of increasingly globalised world. Also there is a potential danger of very conservative scholars with an insular mind set creating unnecessary complexities just to avoid any engagement with non-Islamic companies.

*“Shariah scholars can be biased and take rigid decision which is entirely negative to the development of the organization, and managers can’t do anything about it”. [P8-B-UAE]*

#### **4.6.2 Special Way of Dealing by Non-Islamic Companies**

Majority of respondents agree to the view that Western companies are willing to work with Islamic companies in the Gulf countries with great care and that they have an adequate understanding of the need to comply with the *Shariah* principles. Further, the interview analysis showed reinsurance practices in these countries are at nascent stage of development and that many Islamic insurance companies deal with reinsurance cases with the principle of *donation* to help them manage risk in collaboration with non-Islamic insurance companies. This practice signified an understanding of the need for trade-off when working with non-Islamic insurance companies.

It was found that Western companies treat Islamic companies in the Gulf countries with great care, as they are aware of the need of *Shariah* compliance by the Islamic companies and therefore develop an appreciation of the *Shariah* principles to ensure that these are complied with or identify an acceptable work-around for the purpose of the transaction. For example, a respondent from insurance company in Kuwait said:

*“The international companies have begun to understand our need for Shariah compliance. Thus they deal with Islamic companies in a special way to incorporate the principles of Shariah, as they are aware that we always stay away from business operations, which have been prohibited by Islam”. [P9-Ins-KW]*

For example, financial instruments such as bonds, swaps, futures and forwards are not allowed by *Shariah* in their conventional form and would need restructuring, where possible, to comply with the *Shariah* principles, for example, *Sukuk* (Islamic bonds), where the bond is backed by real asset and the return being a fixed share of profit, is always *Halal* rather than the return being in the form of interest, which is *Haram* (Derigs & Marzban, 2008). As Maswadeh (2014) noted, not everything is explicitly prohibited by the *Shariah* and there is scope for interpretation to enable such restructuring. The respect for *Shariah* laws and principles reflects the willingness of foreign companies to do business with Islamic companies. One of the respondents said:

*“Mostly, there is no problem in complying with Shariah governance code except the difficulty faced by the Islamic insurance companies in the reinsurance sector. The Islamic companies have no readily available Islamic alternative to the reinsurance”.* [P12-Ins-SA]

The practices of reinsurance in the Gulf countries are relatively new (Mulhim & Sabbagh, 2007) and they lack the human and infrastructural capability in dealing with the *Shariah* compliant reinsurance capacity to help manage excess risk (Vizcaino, 2015). There are no reinsurance companies in SA, forcing its *Takaful* insurance sector to deal with non-Islamic companies for reinsurance, which is not ideal from Islamic insurance point of view. The UAE *Takaful* insurance sector has, however, developed a workaround:

*“We are dealing with reinsurance companies on the principle of donation to cover accidents. When we deal with non-Islamic reinsurance companies, we work against Shariah principles and one way to avoid this is for the Takaful insurance company to normally hold 40% share based on the interest free dealings while the 60% is held by the non-Islamic company, which can invest on interest based transactions. Takaful*

*insurance company does not share any profit through 40% ownership but requests a lower level of donation in the next period contract. So there is always trade-off when combining Islamic and non-Islamic practices”.*

[P2Ins-UAE]

The above comment suggests that the non-Islamic companies are agreeable to necessary practical adjustments as long as the Islamic companies have identified the required restructuring of the business, instruments or products to ensure *Shariah* compliance.

#### ***4.6.3 Complexities of Merging Islamic and Non-Islamic Practices***

In quite contrast to the above finding, majority of the respondents believed that it is hugely complex, costly, and problematic to restructure products and services in order to make them comply with *Shariah* principles when working with foreign companies. Factors such as lack of appropriate infrastructure and, the discretionary power of the *Shariah* court and *Shariah* scholar subjective interpretations exacerbate the problem when considering the integration of Islamic and non-Islamic practices.

Even conventional M&A involves considerable complexity; however, compliance with *Shariah* introduces even greater degree of complexity when dealing with non-Islamic companies. A respondent from insurance sector in UAE has pointed out some of the limitations arising from *Shariah* compliance:

*“Although doing business by following Islamic principles is good and low risk, it causes difficulties in the cases of restructuring the products to comply with Shariah. If the company did not have to worry about this compliance, it would be more flexible in business and would also find more investment opportunities”.* [P5-Ins-UAE]

Similar view has been mentioned by some of the respondents from the banking sector of SA.

*“M&A activities may face some challenges due to non-compliance of international companies with Shariah laws, but we use only those restructuring transactions, which comply with Shariah, even though we face considerable difficulty in selection of such capital structure”. [P14-BSA]*

The above comments indicate that *Shariah* compliance may be a barrier in dealing with non-Islamic companies. This is similar to IFR (2009), which noted that structuring Islamic company to accommodate capital structure of the target company could be cumbersome, time consuming and costly. In many cases such restructuring might fail leading to breakdown or excessive delays in the M&A process. As it is, the process of cross-border M&A is complex and requires evaluation of a range of business, legal, operational, accounting and tax issues as well as consideration of risks associated with cross-border deals -*Shariah* compliance adds to the complexity and introduces further costs and delays (Rezaee, 2011; Lakshmanan, 2014).

Carrying out the legal due diligence can be problematic as the *Shariah* court has broad discretionary powers in reviewing and interpreting any business documents (Kortbawi, 2014). It also highlights the potential problems that could arise from subjectivity involved in interpretation of the *Shariah* business laws and absence of any objective rules and standards.

#### **4.7 Islamic Corporate Legal Structure**

One of the research questions of this thesis sought to examine the difference in the legal structure of the Islamic companies and its influence on decision making.

Corporate legal structure of company manifests the principles and codes that the company is bound to follow in the conduct of its business operations. This structure is influenced by the national legal system, which in case of Gulf countries is quite complicated as it is embedded in history, religion and traditions of each country (Angell, 2006). CG is based on the legal structure of a company and in case of Islamic

companies *Shariah* plays a critical role in shaping the legal structure of the company (Ararat & Ugur, 2003). An important constituent of the Islamic corporate legal structure is the *Shariah* Supervisory Board. The analysis below addressed the interview questions 2, 5, 6, 11, 14 and 15 from Appendix 4 and interview questions 22 & 23 from Appendix 5.

#### **4.7.1 *Shariah* Supervisory Board**

*Shariah* Supervisory Board (SSB) can be defined as a body made up of a number of scholars who are knowledgeable about Islamic commercial jurisprudence (*Fiqh AlMuamalat*), which issues binding guidelines and supervise their enforcement to ensure *Shariah* compliance (Alkhamees, 2013). Alman (2012) suggested that the SSB should comprise of at least three members, who have understanding of the modern trend in business, finance and economics in addition to the knowledge of the *Shariah* business principles.

The SSB can comprise of either internally employed scholars or externally appointed scholars on a retainer fee basis. In terms of its importance, the respondents from the SA observed:

*“SA does not have any regulatory framework for *Shariah* supervisory practices. The IFIs voluntarily deploy their initiatives like other Gulf countries and the SSB is as influential and powerful as BOD. The BOD has no authority on the functions of SSB. The SSB gives an Islamic advisory opinion called “Fatwa” on every process of the bank or company, and monitors the process and product and matches them with principles of *Shariah*. Finally it issues the annual report to the shareholder in general assembly regarding following and implementing the *Shariah* based legal structure”. [P4-B-SA, P6-Ins-SA]*

Lahsasna (2011) affirmed that the SSB always ensure the full compliance and implementation of *Shuratic* decision-making. Grassa (2013) and Grassa & Matoussi (2014) have noted that Bahrain has developed a comprehensive regulatory framework, which may encourage other countries to do so. In terms of the relationship between SSB and BOD, the SSB may be seen in terms of providing guidance and stewardship. Bhatti & Bhatti (2010) emphasised that stewards are more inclined to perform their duties in the spirit of partnership. Similarly, Turnball (2000) pointed out that experts and specialist are employed by organisation for better results.

#### ***4.7.2 Selection Criteria and Number of Shariah Supervisory Board***

It was found that Gulf countries follow different mechanisms and rules in selecting the members of the SSB, thus creating differences in the legal structures among the Gulf countries. For example, in SA, the company's leadership such as BOD makes the rules and regulations, and are responsible for the formation and selection of the SSB members. One of the respondents from the banking sector of SA reported that:

*“Some companies assign the SSB members through voting in the general assembly. This is the typical situation in assigning according to AAOIFI standards. These standards are adopted in some countries and used as a reference in others. However, in Saudi they are not used either as compulsory or as a reference standard. In some countries, the selection of SSB members is mediated by CEO or by the BOD”. [P3-B-SA]*

Another respondent noted:

*“The role of SSB is only legislative and their meetings with the BOD are held once or twice monthly based on the necessity such as new deals or new contracts. Their authority is equal to the BOD in exercising the decisions in the legislative domains of the company. The reputation, knowledge of jurisprudence and the experience of the SSB members are*



*also included as an essential criterion for selection of the members of SSB”. [P3-B-KW]*

The above comment suggests that there are variations in legal structure and responsibility among Gulf countries. The AAOIFI standard states that BOD members are responsible for the appointment of the SSB members and the appointment requires approvals from the shareholders in the General Meeting, however, not all Gulf countries follow this standard. As Farook & Farooq (2013) pointed out there is economic gain in having *Shariah* scholars on the BOD to benefit from their expertise and experience and thus reduce the times required in ensuring *Shariah* compliance process. This would also benefit the *Shariah* scholars in terms of obtaining greater business understanding. Archer & Karim (2007) noted that there are many *Shariah* scholars who have published on commercial jurisprudence without the day-to-day practical experience on modern banking and financial markets.

Since the composition and appointment of SSB members vary from institution to another, the credibility of the decisions made by the SSB is affected. The majority of the respondents believed that increase in the number of the SSB members could strengthen the legal structure of the company in terms of forming transparent and lucid regulations to control the development of financial instruments of the companies. For instance, one of the respondents from the insurance sector quoted that:

*“More members can increase the quality of decisions; this is because of the fact that it will eliminate the chance of collusion between the members to compromise the Shariah and the business interests. The more members will increase the degree of differences in opinions between members, and ultimately result in better quality of decision than having fewer members to have monopoly over the decisions”. [P8-B-SA]*

Hasan & Laws (2007) and Alman (2012) noted that the concept of having more than one member on the SSB is very important to eliminate unilateral decisions and ensures adequate discussion of issues for reaching a collective decision.

Therefore, there is a need to establish clear rules and regulations defining the composition and detailed selection criteria for SSB that is better understood by all stakeholders. With the very important role of SSB in directing and reviewing activities of Islamic companies, there might be negative effect on the company's performance if the SSB members are not well versed in the modern business and economic practices, besides any problems that might arise in harmonisation with non-Islamic companies.

As a summary of the above two sub-sections, it could be stated that almost all respondents agreed in their views that *Shariah* Supervisory Board to be influential and powerful constituent of the Islamic corporate legal structure with mandate of providing Islamic advisory opinion called "Fatwa" on processes, products and service to ensure they comply with the principles of *Shariah*. The data analysis however, showed the three countries differed in the processes of selecting the members of the SSB and that not all the three countries follow the AAOIFI standards when appointing the SSB. Thus, the respondents argued for establishing transparent rules and regulations defining the composition of, and selection criteria for SSB.

#### **4.7. 3 Adoption of (AAOIFI) Guidelines**

Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) provides guiding standards that the Islamic companies can follow in ensuring that they are in compliance with *Shariah* (AAOIFI, 2004). Some organisations fully follow these standards while others use them as a reference when making particular decisions. These comments are supported from the banking sector in the UAE and Kuwait. One of the respondents from the UAE commented like that:

*"AAOIFI works to formulate the different rules and regulations, which may be obeyed by the financial institutions to develop and regulate the products in the market. The SSB members use these rules as guidelines for*

*approving the Islamic products in banks. However, they are not compulsory”.* [P7-B-UAE]

Since the adoption of the AAOIFI standards is not universal, it leads to a range of Islamic organisational structures, for example, some organisations have only a single tier comprising of SSB and at the other extreme other companies have three tiers consisting of SSB, internal *Shariah* audit and external *Shariah* audit for ensuring *Shariah* compliance. A respondent from the banking sector in the UAE explained the current state of play as:

*“In some banks and companies in UAE, there is Shariah Board and internal Shariah audit. Nowadays external Shariah auditing has also been implemented. Internal auditing on the SSB to supervise the functions of SSB has also started in Kuwait and Bahrain”.* [P11-B-UAE]

The forgoing comments have revealed the important aspects of the regulatory mechanism in the Islamic banks and insurance companies in the UAE and Kuwait. The three tier structure comprising of SSB, internal and external audit provides additional supervision on the activities of SSB as well as compliance to SSB decisions by the management. This makes it a robust structure for compliance of business operations with the injunctions of *Shariah*. Such architecture of ensuring *Shariah* compliance has not been implemented in the banks and insurance companies in SA.

#### **4.7.4 Conflict of Interest**

The AAOIFI guideline requires that the SSB appointed members should not hold any shares within the company for which they work, as it creates conflict of interest. By owning shares in Islamic companies, they might be tempted to engage in misinterpreting the *Shariah* principles for the company’s benefit rather than ensuring interest-free and *Halal* principles in the backdrop of socio-economic justice in line with *Maqasid Al-Shariah*. A respondent from insurance sector from SA stated the issue as:

*“If shares have been allocated to the members of the SSB, it will give rise to the conflict of interest. For example, The SSB member with share will work only for his own interest regardless of whether it is within the spirit of Shariah or not. This can affect their interpretation and application of the Shariah principles and also the overall compliance of the company with the Islamic framework”. [P10-B-SA]*

Malkawi (2014) affirmed that an SSB member involved in running the business may result in issues related to confidentiality of information and favourable disposition towards managers with whom they work more closely. Bakr (2002) also noted that the SSB members should not engage in any activity other than their assigned functions or roles in an organisation due to conflict of interest that may arise and it is hard to express an independent opinion when engaged with other jobs or owning shares. Similarly, Qattan (2003) recommended that SSB members should not be assigned any executive position in any of the institution they are involved, as it will impair their independence.

Members of *Shariah* board were asked about the possible conflict of interest when using an external *Shariah* scholar (see questions 7, Appendix 4). Potential conflict of interest may arise when Islamic companies do not have SSB constituted by internal employees but depend on external experts on a retainer basis. Garas (2012) highlighted the problem of external members sitting on different companies' SSB having access to a lot of confidential information which might could lead to potential losses for some companies and gains to other companies in which they might have interest.

One respondent also highlighted the conflict of interest in case of scholars working as external SSB members and suggested that the scholars on the payroll of the Government, serving as the *Fatwa* Council members should issue an impartial, free, advice to Islamic companies.

*“The Government is so fair, equitable, and clear, and this is what the Islamic religion urges, but unfortunately, the principles are applied outside more than inside the country. I don't think that the SSB have any role; they are just committees depending on robbery of money as they do not make decisions until they take money because this money affects their judgments, why they do not just sit at the Government's Fatwa Council and issue free advice? Why they are working in companies? Why they take money for Fatwa granted from heaven? Money plays a crucial role in the Fatwa council decisions”. [P11-Ins-SA]*

Therefore, it is important to have clear and well-defined rules and regulations on the composition and functioning of SSB and the rights, responsibilities and obligations of its members in Islamic companies in the Gulf. The above accounts, in part, provided an insight into the questions which asked about managers' perception on the role and impact of SSB in their companies (questions 22, 23 and 26, Appendix 5).

#### **4.7.5 Variation in Structure of Shariah Compliance**

It was found that the SSB members in different Islamic companies had different perspectives on *Maqasid Al-Shariah*, leading to differing interpretation besides the conflict of interest discussed above. The respondents were also of view that there was scope for differing interpretations, for example, a respondent from a UAE bank said:

*“It is quite normal in Shariah to promote the difference of opinions in constructive way. Difference of opinions is considered a mercy. However, the difference in already established and well-practised principles of Shariah is considered a departure from the compliance with the Shariah laws”. [P12-B-UAE]*

Another respondent from insurance sector in SA supports this view:

*“The SSB members are not always clear in interpreting the Shariah principles for any business deals. Any misinterpretation of the SSB*

*members can be seen by the wider public, who have their own understanding of Islamic principles and what is lawful and what is unlawful. It is not good practice for SSB members to give their own interpretations, as this can cast doubts on the legality of any business deals”.* [P7-B-SA]

Hamza (2013) noted that various scholars interpret *Shariah* differently and in some cases there is no definitive answer about the status of *Shariah* business principles, which may lead to uncertainty about what will be acceptable and what will not, complicating inter business activities among companies. Obid & Naysary (2014) supported this view by emphasising that different background and school of jurisdictions of SSB members as well as the national regulatory environment and regional context can create inconsistency in the *Shariah* interpretation and may prevent the harmonisation of products and services. In support of this view are also Dusuki & Abozaid (2007), who noted that the misunderstanding of *Shariah* principles can hinder the implementation process or success of business deals. For example, Beck et al. (2013) explained that it is unclear whether the products and services follow the principles of Islam in terms of form or in terms of spirit (*Maqasid Al-Shariah*).

Therefore, unifying the interpretation of the *Shariah* business principles may aid in the success of cross-border M&A by removing uncertainty about position taken by individual scholars on various issues. The adherence to well defined CG codes and mutual agreement between the companies merging into each other can guarantee the success of the M&A activities and will stabilise the M&A contracts between the Islamic companies in Gulf and other non-Islamic countries.

#### **4.8 Islamic Financial Instruments**

This section presents the findings relating the research question/ objective regarding the main Islamic financial instruments used by Islamic financial companies. One key

question managers were asked was ‘Which Islamic instrument do you use to formalise businesses that comply with *Shariah* across international boundaries?’

Islamic financial instruments are the main funding tools offered by the banks to the investors and other companies to finance their businesses. These are the Islamic alternatives for the investors to either expand their businesses through the M&A or to start new business. The Islamic instruments (based on fundamental *Shariah* principles), which are used to finance the investors include: the profit and loss sharing instruments *Mudarabah*; *Musharakah*; *Murabahah* (cost-plus financing); and *Ijara* (leasing). These basic instruments are then utilised to formulate more complex instruments such as the Islamic Bond or *Sukuk*. While the conventional financial companies engage in interest-based transactions, Islamic companies need to structure financial instruments offering similar capability without incorporating any element of interest.

#### **4.8.1 *Sukuk***

Among all the financing methods available, it was found that *Sukuk* is the most popular and is considered to be fully compliant to *Shariah* business principles. One of the respondents said:

*“The utility of the financial instruments is that they are being used by investors to acquire the funds for the international M&A activities. There are many companies in the Gulf countries, which expanded their businesses through the use of Sukuk which can be either Murabahah or Ijara based. The most popular and successfully used financial instrument is still Sukuk for international M&A deals as it is non-controversial and fully compliant with Shariah”.* [P14-B-SA]

The statement above shows the popularity of *Sukuk* for M&A as it is widely accepted as non-controversial and the most *Shariah* compliant instrument as it has inherent flexibility of being structured using any of the underlying *Shariah* concepts, for example, *Murabahah*. *Sukuk* is quite similar to the conventional bond products such

that the sale of debt is negotiable and where payment can be made by periodic instalment or can be deferred to maturity (Saeed & Salah, 2014). Wilson (2008) noted that Islamic securities are becoming popular lately such that the Government use them to raise Government finance and companies use them to raise fund. *Sukuk* has the advantage over conventional bonds as *Sukuk* is always backed up by real asset such as building, equipment and land.

On fund raising by *Shariah* compliant companies through common stock vs. *Sukuk*, Abaza (2011) observed that *Sukuk* had the disadvantage of widening of credit spreads which makes it less cost effective and the cost of structuring *Sukuk* was still relatively high compared to the conventional bonds and bank loans in most parts of the World. An alternative position, arising from *Sukuk* becoming mainstream and the demand from cash-rich institutional investors often exceeding supply, was in Islamic countries such as the Gulf countries, where the issuance of conventional bonds can be more expensive for corporate than *Sukuk*, however, this was seen as an exception rather than the rule (Al-Amine, 2008; Al-Thani, 2013).

#### **4.8.2 Tawarruq**

Another Islamic financial instrument that is sometimes used for M&A is the *Tawarruq*, which involves cash sales of goods purchased on instalments or deferred payment basis (Ahmad et al., 2009). It was found that some organisations do not recognise *Tawarruq* as a valid Islamic instrument and even among the *Shariah* scholars the status of the *Tawarruq* as a financial instrument is controversial. Some of the respondents commented on *Tawarruq* as follows:

*“Tawarruq involves an individual or company buying a commodity that is not belonging to precious metals category, from a bank on a deferred payment or instalment purchase basis then, reselling it for the purpose of generating cash. The price paid to the bank includes an inbuilt profit margin and is higher than the sale price used to generate cash”.* [P9-Ins-KW]



The same respondent mentioned that:

*“Some financial institutions rejects this concept and hence do not approve the use of Tawarruq as financial instrument, for example, Dubai Bank rejected the Tawarruq as a Shariah compliant structure. However, AAOIFI permits the use of Tawarruq under certain conditions; for example, the client should not delegate the institution or its agent to sell on his behalf a commodity that he purchased from the same institution. However, such approach is not subscribed by some of the financial institutions”. [P9-Ins-KW]*

Another respondent from the insurance sector in SA recorded similar thoughts regarding the use of the *Tawarruq* as a last resort rather than using it as a standard financial instrument:

*“Tawarruq by many Shariah scholars is considered as a necessary evil rather than an important pillar of the Islamic financial services. Both financiers and lawyers believe that there is a gradual movement in Gulf countries demanding the up grading the standards of the Islamic finance. The scholars are increasingly encouraging the Islamic financial institutions to look for alternatives to the Tawarruq, which suggest the stricter standards to which the industry is heading for”. [P6Ins-SA]*

The advantage of *Tawarruq* is that it is flexible and a quicker way of acquiring liquidity (Msatfa, 2011). However, there are issues with *Tawarruq* that have been discussed by various authors due to the different ways in which *Tawarruq* is used by banks. Some scholars argued that if the only objective of the customer is to generate cash and is personally involved in the whole process then it is not prohibited while others argue that

the customer does not really have to be involved in all the business transactions (Ahmad et al., 2009). In the circumstances where the commodity is resold at very low price, *Tawarruq* will be prohibited by *Shariah* scholars (Haneef, 2009) as it is seen as exploitation.

The discussion thus far shows that *Tawarruq* is used by the financial institutions in Gulf region with great caution. The practice may vary from country to country based on the interpretation of *Shariah*. In Malaysia, for example, *Tawarruq* is recommended and approved by the *Shariah* scholars while it is not encouraged in the Gulf countries (Khniifer, 2010). The analysis by one of the respondents from the UAE banking sector provides evidence:

*“Malaysia and Gulf countries are different in terms of approving the Tawarruq structure, therefore the latter is more dependent on the alternative forms of financing rather than Tawarruq. Also, in Malaysia, there are a handful of the other structures, which can be employed to help facilitate Shariah compliant M&A finance”. [P11-B-UAE]*

Focussing on the cross-border M&A between Islamic and non-Islamic companies, there may be plenty of obstacles. For example, one of respondent from the banking sector in SA commented on these difficulties:

*“M&A activities with the non-Islamic financial instruments is complicated for us because we need to convert them into Islamic ones by changing all of their non-Islamic (interest-based) transactions into the Islamic transactions by applying the principle of Tawarruq which means that we need to give all prohibited money (interest-based income) earned by the host bank to the charity. In this case we lose money rather than making the money. Therefore, the use of financial instruments by the host company matters much to us”. [P15-B-SA]*

The respondent from UAE reported similar issue in dealing with non-Islamic banks either in the Gulf regions or in the Western countries.

*“In the case of M&A, Muslim customers who deals with non-Islamic banks are wishing to move their transactions to the Halal transactions (interest-free transactions); we convert debts to the legitimate ones through the use of Tawarruq. The amount of risk is high in such conversion transactions, because the bank acquiring the non-Islamic bank has to pay the amount of debt and extra amount for the final settlement. In order to compensate this; the Islamic banks will have to increase the operating cost up to 20-30%. This will ultimately affect the competitiveness of the Islamic bank in the region. Therefore, it is very less likely that Islamic banks will sign any M&A deals with the non-banks”. [P9-B-UAE]*

This finding is similar to Lakshmana’s (2015), who reported that although the rationale for the conversion might seems acceptable, there is no guarantee that the conversion process will be issue free or runs smoothly. Therefore, the main issues pointed out by the above statements are debt creation and the excessive cost of implementation of Islamic financial instruments involved in removing the non-Islamic financing instruments used by the conventional banks.

The bottom line is that Islamic financial instruments play a key role in facilitating the M&A activities. However, there are some controversies about the legality and validity of some of these instruments due to the challenges in the way of making financial instruments fully *Shariah* compliant and in creating a consensus among the *Shariah* scholars across the Gulf countries to formulate a uniform *Shariah* standard for widely used instruments. The financial industry in the region also needs to innovate and develop further financial products in addition to those already existing, to facilitate cross-border M&A activities. It can be concluded that the use of Islamic financial instrument in the process of cross-border M&A is challenging, and at times, costly, due

to the ways in which the non-Islamic financial companies operate using financial instruments with interest as key profit making instruments, and this situation requires balancing the trade-offs by both parties.

#### **4.9 Chapter Summary**

The purpose of this study was to investigate the influence of *Shariah* CG on cross-border M&A in three Gulf countries (Saudi Arabia, Kuwait and UAE) and to contribute to the literature by enriching the existing literature on CG and exploring the differences in the *Shariah* CG practices and mechanisms within three Gulf countries. This chapter presented results and analysis of the data collected from interview with 40 respondents from 15 financial institutions in three Gulf countries. Three categories of informants (lawyers, *Shariah* board members/*Shariah* scholars and managers) with hands-on knowledge, experience, and expertise on the topic of the study were interviewed. The key findings indicated the emergent nature of Islamic CG principles; how the required compliance to *Shariah* laws and principles, and differences in interpretation of the *Shariah* principles by *Shariah* scholars could be both enabler and constraining, the underdevelopment of Islamic legal structure and the problematic nature of use of Islamic financial instruments during the cross-border M&A between Islamic and non-Islamic financial companies.

Perceptions of interviewees are consistent with three management theories i.e. Stakeholders' theory, Stewardship theory and Agency theory that impact CG mechanisms including BOD members, SSB members and auditors who play a significant role in facilitating cross-border M&A. However, respondents revealed key obstacles to the success of cross-border M&A between Islamic and non-Islamic companies such as the need for *Shariah* compliance (prohibition of *Riba*, obligation of *Zakat* and Islamic inheritance law), weak system of disclosure, lack of independence, corruption in compliance, existence of family members in the Board, weakened communication with external auditors, different interpretations of *Shariah* by different

scholars, Islamic inheritance law and lack of alternative Islamic financial instruments. The next chapter presents conclusion, implications and ideas for further research.

## CHAPTER FIVE: CONCLUSION

### 5.1 Chapter Overview

This chapter presents summary of key findings, conclusions, contributions and implications of the study. It is organised as follows. Following this Introduction, summary of key findings is presented followed by the main conclusions of the study. Barriers to effective Islamic CG, and Islamic CG are the focus of the conclusions. The study's theoretical contributions are discussed in section four followed by the implications and recommendations in section five. Given the focus of the study, the study implications and recommendations relate to the regulatory bodies, *Shariah* supervisory board, management and investors. Section six identifies and discusses the research limitations and ideas for future studies. The last section presents 'final note on the initial research objectives

### 5.2 Key Findings

This thesis examined the influence of *Shariah*-based CG on cross-border M&A involving Islamic financial companies in three Gulf countries and non-Islamic financial companies from the Western countries. Overall, seven key findings emerged from the analysis of semi-structured interviews with 40 respondents who were purposively selected from 15 financial companies in Saudi Arabia, Kuwait and UAE and the relevant empirical literatures and theories. These findings were:

1. In terms of corporate governance, there were variations among the three countries regarding the extent to which Islamic CG model is adopted and employees are aware of the CG principles, and how the conventional CG model is practised. Whilst Saudi Arabia adopts Anglo-Saxon model with *Shariah*

enshrined in it, both Kuwait and UAE are keen in embracing any CG models in modified form to conform to the *Shariah* principles. In both Saudi Arabia and Kuwait, employees were found to be less aware of the CG principles whilst growing awareness by employees was evident in case of the UAE. Islamic companies found difficulties to applying conventional CG model in Saudi Arabia and Kuwait but such companies were likely to apply the conventional CG model provided that they conform to business practices allowed by *Shariah* principles. All the three countries do not have written code of practice but the compliance with the *Shariah* principles is a must.

2. In terms of CG mechanisms, both Saudi Arabia and Kuwait tended to have weak system of disclosure (in particular *Zakat*), and small board dominated by family and less qualified members. In contrast, high level of disclosure and larger, diversified and competent board exist in the UAE. In addition, whilst companies in UAE use three layers of compliance through SSB, internal and external *Shariah* auditors, SSB and Internal auditors in Kuwait and only SSB in Saudi Arabia are used as mechanism to ensure compliance to *Shariah* principles and transparency.
3. Incorporating Islamic principles in business practices such as screening provision of products and service in these three countries is primarily determined by the interpretation of *Shariah* by internal *Shariah* Board or external *Shariah* audit or by both. However, the study found the importance of having in place appropriate legislative provision for effective application of *Shariah* laws as the three countries adopted different stances from passive (market-driven in Saudi Arabia) , minimalist intervention of law ( Kuwait), to ensuring compliance with external *Shariah* audits in UAE. However, this study found that all the three countries' companies are open to idea of adoption of Islamic products on a larger global level.

4. The taken-for-granted views regarding the family inheritance, women and business, the study found, are likely to influence negatively the extent to which some aspects of the Islamic CG is to be practised and become effective. For example, gender differentiation and the dominance of family members in board were likely to lead to lack of diversity in Board composition and experience and hence negatively affected the effective use of CG principles. The reported poor understanding of the Western business concepts, in Saudi Arabia and Kuwait in particular, is likely to influence how successfully the initiatives seeking cross-border M&A between Islamic and non-Islamic financial companies could be undertaken. Women in the SA faced work place segregation when compared women in Kuwait and UAE.
5. The three countries differed in the ways in which companies could be impacted because of the ways in which Shariah scholars interpret sharia law in reference to business practices. The findings of this study showed that Saudi Arabia is typified by most conservative interpretations whilst Kuwait and UAE tend to have more liberal and most liberal, respectively, interpretation of the *Shariah* principles. Furthermore, both Saudi Arabia and Kuwait companies had to go through complex procedure as compared to complex but flexible approach in UAE, when dealing with M&A issues with non-Islamic companies. Though this study documented evidences which suggest an increasing number of non-Islamic financial companies are cognizant of the need for compliance to *Shariah* principles, they need to understand how the countries' context affects the Islamic financial companies' ability and latitude when seeking cross-border M&A activities with non-Islamic companies.
6. Islamic corporate legal structures in the three countries are characterised by similarities and differences in *Shariah* supervisory board composition and selection, adoption of AAOIFI guidelines and issues relating to conflict of interest. In SA and Kuwait most Islamic financial companies have SSB made up of external scholars whereas internal SSB made up of scholars features in UAE



companies. Boards tend to have no fixed size and being appointed by BOD or CEOs in both SA and Kuwait whilst shareholders select SSB in UAE. In all the three countries, AAOIFI standards are not considered mandatory for adoption but serve as a reference when dealing *Shariah* compliance issues.

7. In terms of Islamic financial instruments, *Sukuk* is the most widely used but costly financial instrument in cross-border M&A activities as it fully complies with *Shariah* principles where as *Tawarruq* is considered questionable in terms of *Shariah*.

**Table5-1: Table of Findings**

SN	Theme/Sub-Themes	Saudi Arabia	Kuwait	UAE
	Corporate Governance (CG)			
1	Adoption of Islamic CG model	Mainly follow Anglo-Saxon model with <i>Shariah</i> enshrined in it.	Willing to adopt any CG model that can be modified to comply with <i>Shariah</i> principles.	
2	Code of practice	No written code of practice but compliance to <i>Shariah</i> principles is based on the interpretations of <i>Shariah</i> scholars.		
3	The degree of awareness of CG principles	Most employees are not fully aware of Islamic CG and there is no effort by the Government to increase the awareness.	Most of the employees are not fully aware of Islamic CG as the concept is seen as quite recent and new.	There is a growing awareness of Islamic CG in the UAE and many companies actively undertake periodic appraisal to improve it.
4	Applicability of conventional CG model	Cannot be applied directly to the Islamic companies due to strong religious and cultural beliefs.		Can be applied but with modification of areas that clearly violate requirements of <i>Shariah</i> .
	Corporate Governance Mechanisms			
5	Disclosure and transparency	Weak system of disclosure, especially <i>Zakat</i> , which can be improved by better qualified and experienced SSB.  Payment of <i>Zakat</i> is compulsory.		Higher level of disclosure due to involvement in international environment.  Disclosure and payment of <i>Zakat</i>
				is optional.

SN	Theme/Sub-Themes	Saudi Arabia	Kuwait	UAE
6	Board size and characteristic	Board are small (usually family members), members might not be suitably qualified and rarely women can be included based only on ownership.		Bigger and better  Qualified Board with members from diverse backgrounds, including women and foreigners.
7	Ensuring <i>Shariah</i> compliance and transparency	Compliance only through SSB. No <i>Shariah</i> internal or independent external audit leads to poor transparency.	Compliance through SSB and <i>Shariah</i> internal auditors, however they might lack financial and economic knowledge. Also, no independent external <i>Shariah</i> audit leads to inadequate transparency.	Three layers of <i>Shariah</i> compliance through SSB, internal <i>Shariah</i> auditors and independent external <i>Shariah</i> auditors with better qualifications and experience ensures greater transparency.
<b>Incorporating Islamic Principles (<i>Shariah</i> law) in the Business</b>				
8	Scope of International M&A	Adoption of Islamic products is not limited to Islamic countries as there are potential customers even in non-Islamic countries.		
9	<i>Shariah</i> screening of products, services and transactions	Compliance based on the interpretation of <i>Shariah</i> by internal <i>Shariah</i> Board or external consultants.		As in case of SA and Kuwait, but increasing subject to external <i>Shariah</i> audit.
10	Legislative provision	No legislation. Passive approach,	Minimal intervention but law	Ensure <i>Shariah</i> compliance

		Letting market develop its own <i>Shariah</i> governance system.	requires Islamic companies to comply with <i>Shariah</i> .	through external <i>Shariah</i> audit.
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SN	Them/Sub-Themes	Saudi Arabia	Kuwait	UAE
	Cultural Influences			
11	Islamic inheritance law	Shariah clearly defines the law of inheritance based on composition and gender of family members. Family size tends to be larger with an average of 7 to 8 children which compounds the number of owners through inheritance.		
12	Women at workplace	Women are not allowed to work in the same places with men.	Women work in the same places but at lower levels and there is legislation to protect women from harassment.	Women work in the same places and at all levels with men.
13	Business culture and decision making	Lack of investment culture. Poor understanding of Western business concepts. However, in insurance sector there is better engagement with non-Islamic companies.		Better business culture and understanding but threat of increasingly negative perception of Islam post 9/11 and European refugee crisis.
	Need for Shariah Compliance in M&A			

14	Effect of <i>Shariah</i> scholars' interpretation	Most conservative in adherence to <i>Shariah</i> principles and have poor understanding of non-Islamic business concepts.	More liberal than SA in the interpretation of <i>Shariah</i> principles but have poor understanding of non-Islamic business concepts.	Most liberal in the interpretation of <i>Shariah</i> principles and provide training in modern business concepts to their <i>Shariah</i> scholars.
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SN	Theme/Sub-Themes	Saudi Arabia	Kuwait	UAE
15	Special way of dealing by non- Islamic companies	Non-Islamic companies are becoming aware of the need for <i>Shariah</i> compliance by Islamic companies and are developing better appreciation of the principles to help compliance or identify acceptable work-around.		
16	Complexities of merging Islamic and non-Islamic practices	Have complex procedures in dealings between Islamic and non-Islamic companies in respect to M&A, compounded by the subjectivity in <i>Shariah</i> interpretation.		Have complex procedures but these are more flexible and adopt more liberal approach.
	Islamic Corporate Legal Structure			
17	<i>Shariah</i> Supervisory Board (SSB)	Most Islamic companies have SSB made up of external scholars.		UAE mostly has internal SSB made up of scholars employed by company.
18	Selection criteria and number of <i>Shariah</i> Supervisory Board	No fixed size. BODs select the SSB members.	No fixed size. BODs or CEOs select the SSB members.	SSB members elected by shareholders based on BOD recommendation.

19	Adoption of AAOIFI guidelines	AAOIFI standards are not mandatory for adoption by Islamic financial institution but serve as useful guidelines in case of all <i>Shariah</i> compliance issues.		
20	Conflict of interest	<i>Shariah</i> Board members are expected not to have shares or display traces of their own interest. However, this cannot be ruled out in case of external SSB members due to monetary remuneration.		
21	Variation in structure of <i>Shariah</i> compliance	Different interpretations as a result of <i>Shariah</i> scholars' views, especially in the context of poor understanding of business issues.	Different interpretations can exist but process of agreement across the three layers of compliance ensures more standard decisions.	
SN	Theme/Sub-Themes	<b>Saudi Arabia</b>	<b>Kuwait</b>	<b>UAE</b>
	<b>Islamic Financial Instruments</b>			
22	<i>Sukuk</i>	<i>Sukuk</i> is the most popular financial instrument and it was structured based on <i>Shariah</i> principles with regard to cross-border M&A, as it is non-controversial and fully compliant with <i>Shariah</i> .		
23	<i>Tawarruq</i>	The concept of <i>Tawarruq</i> is considered suspect in terms of <i>Shariah</i> compliance and is frequently rejected by scholars who are increasingly encouraging Islamic financial institutions to look for alternatives to the <i>Tawarruq</i> structure.		

## 5.3 Conclusion

### 5.3.1 Main Barriers to Cross-Border M&A

Focusing on the findings summarised in the table, the following are the key obstacles to the success of cross-border M&A between Islamic and non-Islamic companies:

The first barrier is the need for *Shariah* compliance. Since the conventional CG model does not lend itself readily to Islamic companies use, it needs to be modified. The main challenge to overcome is the elimination of all transactions involving interest payables and receivables. As *Riba* or interest is prohibited in Islam, all interest-bearing transactions have to be replaced by a *Shariah* acceptable alternative. There is a multiplicity of practices and even some tolerance of interest when this is replaced by donation of the same amount to charitable causes. The process is costly as it consumes a lot of time and effort. Both the Islamic and non-Islamic companies are required to know what is allowed and not in order avoid confusion and delays. However, this is proving difficult as there is no commonly accepted code of practice for *Shariah* CG and as interpretations of the sharia principles by *Shariah* scholars vary across the countries, with UAE being most liberal and SA being most conservative.

The second barrier related to the weak system of disclosure, found in SA and Kuwait due to low level qualification, experience and insular business practices while UAE has high level of disclosure due to involvement in an international environment. One area of deficiency is the information on *Zakat*. Even for the conventional cross-border M&A, dual taxation is a problem (Di Giovanni, 2005), which manifests in the form of *Zakat* and corporate tax or even dual-*Zakat* in the Islamic context. In SA and Kuwait, *Zakat* is compulsory and collected by the Government. In UAE, however, payment and disclosure of *Zakat* is optional and hence this barrier does not exist.

A third barrier common to all the countries arises from the Islamic inheritance law, under which the business is transferable to the closest blood relations of the business owner, in a quite complex manner based on the composition and gender of the family members (See

Appendix 1). Compounded with the relatively larger family size in Gulf countries (Hamadeh et al., 2008), this can create fragmentation of ownership, allow members with insufficient knowledge and experience on the BOD and create uncertainty of future ownership structure for non-Islamic companies.

Fourth, a strict gender-segregated working environment is also a significant barrier in case of Islamic companies in a conservative environment as M&A with non-Islamic companies will have to contend with the values of equality and diversity in the workplace and even female executives in senior roles. Also, implementing *Shariah* principles on non-Muslim employees may create resistance, for example, when there is condition to cover their head.

The fifth constraint is the lack of alternative Islamic financial instruments to fund M&A as the most popular *Shariah* compliant instrument is *Sukuk*, which involves a much higher cost compared to the conventional bond and bank loan. Islamic companies incur substantial costs in converting an interest-bearing loan to *Sukuk*. Also, because *Sukuk* is asset backed in terms of the value of the asset as well as revenues generated by the asset, the *Sukuk* holder faces a potential risk of sharing a loss if the asset generates a loss. The alternative sometimes used is *Tawarruq*, which is controversial and has been rejected by many *Shariah* scholars. There is a need for innovative and more cost effective *Shariah* compliant financial instruments.

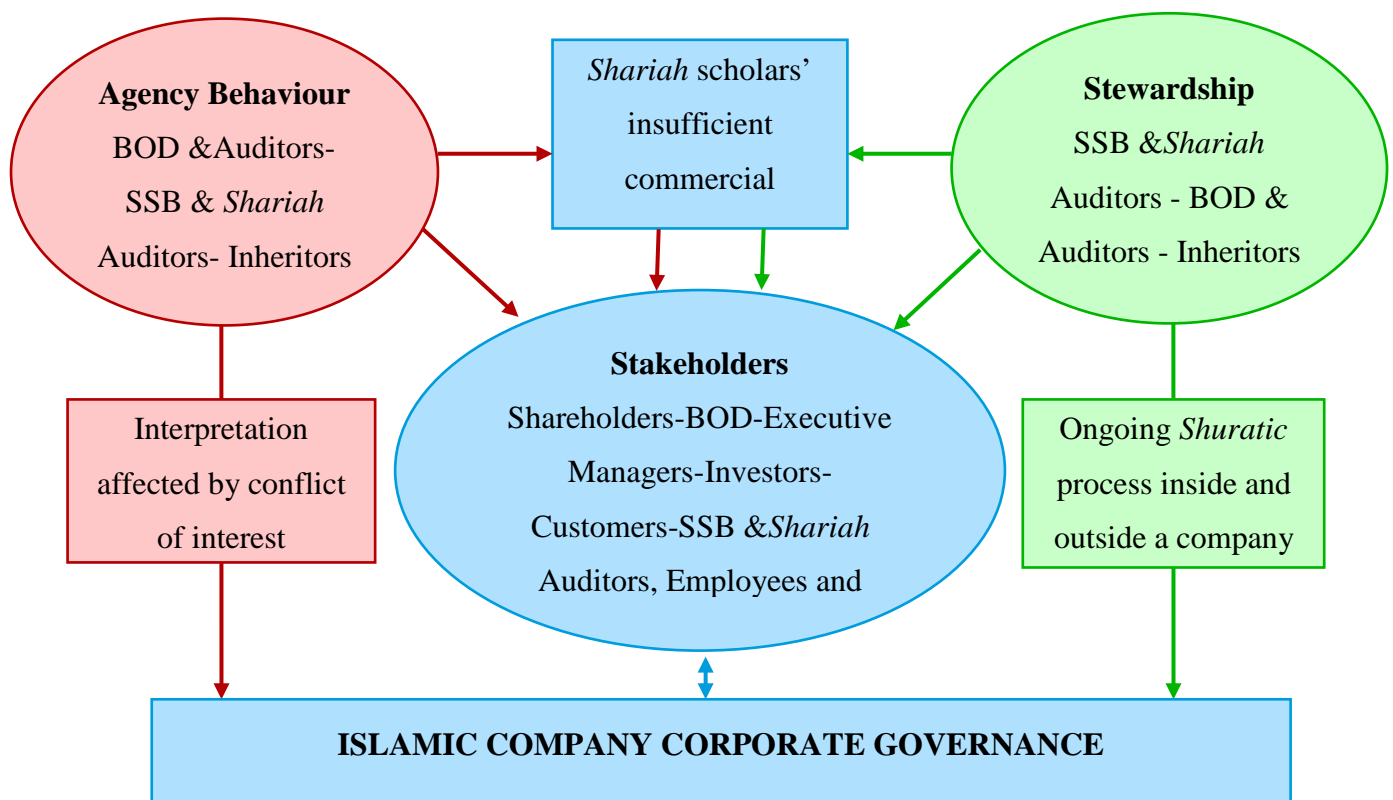
Finally, absence of uniform, standardised, interpretation of *Shariah* laws/principles is also found to be very problematic. As it stands currently, different scholars could provide different interpretations. On one hand, there is flexibility of interpreting *Shariah* to suit different circumstances in different countries, which may be misused as a manifestation of agency behaviour. On the other hand, this could create challenges in an increasingly global world, requiring more uniform and predictable approach. Relatedly, in case of SA and Kuwait, SSB members have insufficient knowledge about and in some cases even lack any motivation to understand conventional business practices and hence not able to question the validity of the interpretations. In extreme cases, scholars with an insular outlook might even introduce unnecessary complexities just to prevent an Islamic company not to successfully engage with a non-Islamic company.



### 5.3.2 Corporate Governance Model for an Islamic Company

Based on the above discussion, it would be useful to consider a CG model for an Islamic company to fully appreciate the possible behavioural issues that may arise out of the need and mechanism for *Shariah* compliance on cross-border M&A. This is particularly important as most of the existing literature on Islamic finance or Islamic way of conducting business is found to be uncritical and promotional in nature, readily identifying potential good systemic practices but not evaluating the role of human actors in sufficient depth to identify possible behavioural problems arising from the compliance mechanism.

Figure 5.1 Islamic Company CG



The model above links three management theories offering two opposing perspectives on the possible behaviour of the stakeholders in terms of CG within Islamic company generally and especially in the context of cross-border M&A. Stewardship theory is an idealistic theory based on the view that the business executives are stewards of the business and therefore have a behaviour that transcends individual gain or self-interest through self-discipline. In the context of an Islamic company, those who are entrusted to ensure *Shariah* compliance are presumed to act objectively at the highest level of ethical values as emphasised by *Maqasid Al-Shariah* and implement the compliance fully in terms of both the letter and spirit. Parallel to the BOD is the SSB, composed of one or more Islamic scholars, who may be externally or internally appointed to carry out assessment of all existing and newly proposed products, services and operations of the Islamic company.

The implementation of *Shariah* compliance is supported by *Shariah* internal auditors in some companies to ensure that the SSB decisions are appropriately carried out. In UAE, we also see the introduction of external *Shariah* auditors to independently confirm *Shariah* compliance. Since the decisions may have to be made in the context of novel products and situations, the different layers provide an opportunity of interaction and dialogue. Such a *Shuratic* process of consensual decision making is allowed and indeed encouraged as stated in *Qur'an* in *Al-Shura* (42:38). In case of externally appointed SSB members who serve on the SSB of multiple companies, there is an opportunity to interact with diversity of opinions solving a broad range of problems in different commercial backgrounds and differing circumstances in an ongoing *Shuratic* process. This can ensure more uniform *Shariah* compliance and help in development of new and better Islamic financial instruments to replace controversial instruments like *Tawarruq* which might superficially comply with *Shariah* in terms of letter but not in terms of spirit.

Even from a stewardship perspective, those involved in ensuring *Shariah* compliance might not be able to take optimal decisions in the interest of all the stakeholders or benefit fully from the *Shuratic* process, if they do not have sufficient commercial knowledge to fully understand the constraints and opportunities offered by commercial context of their decisions. In case of the demise of an owner, there could be a number of successors based on different situations as explained in Appendix 1. However, under the stewardship perspective, the

successors are presumed to act in the best interest of the business and are not likely to pose any challenge other than the fragmentation of ownership and the possible costs and delays involved in decision making.

A potential problem that could arise from the complex Islamic inheritance law relates to the BOD of non-Islamic company, who in their role of the steward for their stakeholders might find it difficult to contend with the uncertainty of succession in case of the demise an Islamic company owner.

However, Agency theory is an opposing perspective to Stewardship theory, where the nature of human behaviour is taken into account, especially when managers as agent of the owner act to maximise their own individual gains even at the expense of the owner and other stakeholders. In the context of an Islamic company, in addition to BOD, the SSB also manage the affair of the company and share in the full authority to implement all business strategies, plans, compliance and decisions. The SSB provide *Shariah* advisory and consultancy to BOD in all aspects relating to product, services and business transactions to be *Shariah* compliant.

The SSB members issue *Fatawa* on a particular commercial issue and the advice can be different based on different interpretation of relevant *Shariah* principles. However, they may have insufficient commercial knowledge and experience, which might affect their decisions. The BOD can influence the SSB members to be favourably inclined towards the BOD's decisions because they determine the consultation fee or the remuneration. Since the remunerations of the SSB members and the *Fatawa* issued by them are not made public, unlike the BOD, it is difficult to make the SSB members accountable by ascertaining the originators of the decisions and identifying who could have influenced the decision. This is a weakness in *Shariah* CG in terms of disclosure and transparency.

The SSB members might be working with many companies due to limited number of qualified *Shariah* scholars (Ali & Al-Aali, 2015). The effect of the memberships on multiple SSB might lead to inadequate time to allow for proper analysis and consideration of all

relevant issues. This also could lead to rush decisions, which might not be optimal. Another drawback is the risk of leakage of a company's confidential information to another company by the SSB members, either inadvertently or deliberately for personal gain. Membership of multiple SSB might also lead to 'group think' behaviour creating a barrier in independently judging situations. There is no regulatory body that provides a code of practice on privacy and sharing of information to inform, govern and penalise the behaviour of the *Shariah* scholars serving on multiple SSB (Bakr, 2001).

Similarly, the possibility that the external or internal *Shariah* auditors, who ensure implementation of *Shariah* compliance, might co-operate to protect each other's interest cannot be ruled out. There are few recognised *Shariah* scholars in the market (Farook & Farooq, 2011; McBain, 2013), who are bound to be familiar with each other and there may also be a pecking order based on reputation, making it difficult to be critical of other scholar's opinions. This can contribute to agency behaviour and weaken the *Shariah* CG model.

When new issues or situations arise in business that are not well defined in the primary sources of Islam *Qur'an and Sunnah*, the SSB members can adopt a secondary source of Islam known as *Qiyas*. *Qiyas* is a deductive analogy, in which the new issue or situation is compared to an existing issue or situation for which there is a ruling based on primary sources and in case of close similarity, the same ruling is applied. However, the SSB might not be able to fully provide an optimal solution due to their lack of understanding of the complexity of the business issues involved.

Also, in case of well experienced SSB members, they may be able to use this lack of knowledge to justify any agency behaviour and offer it as a defence when they are questioned. For example, *Zakat* is a religious tax that is payable on growing capital as well as real assets. The payment of *Zakat* is compulsory in some countries such as SA and Kuwait, while in some countries it is voluntary such as in UAE. The SSB is entrusted with the task of determining the *Zakat* payable. However, the BOD might provide inaccurate financial data to reduce the *Zakat* and the SSB members, not having business knowledge, may not be able to challenge it. Alternatively, the *Shariah* scholars may collude with BOD in order to disclose

lesser amount of *Zakat*, especially if the organisation is financially unstable or to reduce the financial burden on the company. In this case, the SSB members can still offer the lack of business knowledge as a defence. Underpayment of *Zakat* may be as prevalent as underpayment of taxes in conventional businesses.

Also, in case of the demise of an owner, there could be a number of successors depending on different situations (see Appendix 1), fragmenting the ownership. These successors may not work in the best interest of the business and may demonstrate agency behaviour by trying to maximise their own gain.

Whilst on the surface, an Islamic company would appear to be more and better regulated due to an additional Board level managerial control through SSB and the *Shariah* auditors, who are guided by religious conviction in theory. This would indeed be the case if all the concerned parties acted as stewards of the business in the interest of the stakeholders and in the wider societal interest as required by Islam. However, behaviour aspects of human beings cannot be discounted and the presumption of stewardship needs to be carefully examined. In reality, an Islamic company may offer greater opportunities for agency behaviour compared to a conventional company and the literature on Islamic Governance may have to be more critical than currently available to capture some of these complexities.

## 5.4 Original Contributions

This study makes five significant theoretical contributions. These are:

1. The first contribution of this thesis that it is the first of its kind that sought to study the influence of the Islamic CG principles on cross-border M&A between Islamic and non-Islamic financial companies. In doing so, this study contributed in furthering scholarly understanding of: 1) what constitutes Islamic CG and how it differs from the conventional CG models; 2) how and to what extent Islamic CG is practised and its limitations; 3) compatibility and challenges in accommodating various stakeholders'

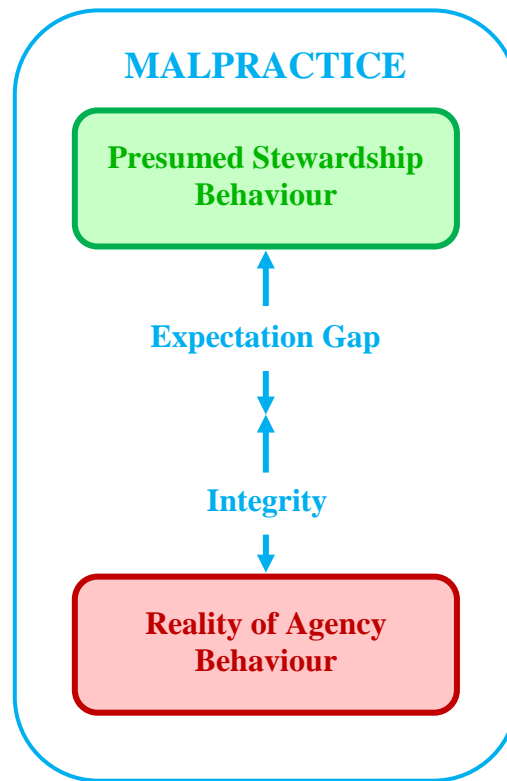
interest in enforcing *Shariah* compliance; and 4) issues needed to be considered for successful cross-border M&A between the Islamic and non-Islamic companies.

2. The second contribution of this thesis is the development of the CG model which helps to further our understanding of the complex issues involved in the process of cross-border M&A between Islamic and non-Islamic companies. As far as this researcher's knowledge, this CG model is the first of its kind in the study context. This CG model can be used by scholars to examine not only cross-border M&A activities across different industries but also more broadly the ways in which the Islamic CG principles, enforcement mechanisms, transparency and disclosure, and accountability are shaped by larger contextual factors such as culture & religion. Better scholarly understanding of the above issues could inform timely and appropriate policy and business practices in the study area and thus may improve the GCC countries firms' experience in globalised business environment.
3. The third contribution of the study to extend agency, stewardship and stakeholder theories in view of the development of behavioural *Shariah* CG model in critical manner. Whilst the stakeholder approach is likely to provide holistic perspectives in informing the expectations, behaviour and actions of different stakeholders, the agency and stewardship by different interest groups could also play an important role in enabling or constraining the firms' motivation and ability to expand internationally or nationally. The existence of additional layer of the Islamic CG consisting *Shariah* scholars, the SSB, internal and external *Shariah* auditors, as agent and stakeholders, could complicate the Islamic CG as they tend to have more latitude and opportunities for agency behaviour compared that is possible within a conventional CG framework. In relation to stewardship theory also the inheritance practices of these countries are less likely to promote the interest of owners in case of cross-border M&A context. This suggests the Islamic CG to be more critical in its stance. Thus, this study provided critiques on the existing literature on Islamic finance or Islamic way of conducting business by identifying both positive and negative practices as well as elucidating the behaviours and actions of different stakeholders. The implication is that use of multiple lenses along the contextual factors is important if we want to understand the companies' (stakeholders') behaviours and the potential consequence

of their behaviours. The study result can be useful and applicable to contexts where Islamic *Shariah* principles have significant influence on business activities.

4. Fourthly, the study identified gaps in the existing Islamic CG model, in particular the difficulties of knowing deficiency of the advice provided regarding *Shariah* compliance, underdevelopment of relevant infrastructure, inadequate or limited business knowledge by management, BOD, SSB and *Shariah* scholars of the Western business context and under defined or emergent legal provisions in support of *Shariah* principles, low level awareness of the conventional CG and its code of conduct and possible cause of variations in *Shariah* compliance which highlighted the difference between the presumed stewardship behaviour and the reality of agency behaviour . Such identification of the limitations of the current Islamic CG models helped to draw relevant implications for various stakeholders (see section below).
5. The fifth theoretical contribution is what might explain the gap between rhetoric and reality of stewardship and agency problems in the study context. This study identified malpractice as source of lack of integrity of agents (e.g., corrupt or selfish *Shariah* scholars or collusion between the BOD and SSB members to gain unfair advantages) and such situation heightens the **expectation gap** between what is presumed and what can reasonably be presumed for a human being (see figure 5.2 below). The below figure shows a range of different individual behaviours to represent an **integrity gap**, where the outcomes will depend on individual or a group's collective integrity. Therefore, malpractice can theoretically be modelled as:

**Figure 5.2: Malpractice**



While this theoretical construct has been derived for the Islamic CG, it is equally valid for the conventional CG, where respect for professional or social status may cloud judgement about the expected stewardship behaviour of individuals in position of authority and the varying levels of integrity demonstrated by such persons individually or collectively. This study thus contributed in identifying ways of mitigating such agency behaviour by: 1) having a larger size board; 2) practising consultative, participative, consensual decision making in line with Shariah guidance, *Shura* (stakeholder consultative participation) process justified by the epistemology of *Tawhid*, meaning oneness of God and hence unity of knowledge (Choudhury & Hoque, 2006).

The analysis of the different theories such as agency, stakeholders and stewardship theories in relation to cultural and religious perspectives examined in the study help to show how these theories can help us in grasping the possible behavioural variations between the ideal and the reality of Islamic CG. Therefore, researchers are encouraged to examine any additional theories that may help in understanding the unique features and practices of Islamic



companies and contribution these can make to the wider management, organisational and even corporate social responsibility literature.

## **5.5 Implications and Recommendation**

### **5.5.1 For Regulatory Bodies**

Firstly, the results of this study and existing literature showed: 1) the non-existence of universal standards which help to harmonise conventional business practices with the Islamic CG principles and, 2) diversity of culture across Muslim countries make it difficult to construct universal standards applicable to all Muslim countries. The study recommends IFSB and AAOIFI to continue with their efforts of constructing a common standard that will be acceptable to all the Islamic financial institutions and provide a uniform basis for Shariah scholars' interpretation to mitigate subjective and multiple interpretations by Shariah scholars.

To overcome such challenges, the various bodies might need to adopt a multilateral approach in working together to develop an Islamic CG model that is in harmony with the modern times and promoting practices that are beneficial to wider society as enshrined in Islam. Though it may have flexibility to incorporate diverse socio-cultural practices, there may be a need to move away from too much reliance on individual *Fatawa*. This would ensure clear processes of business dealings that would be easier to understand by non-Islamic businesses.

### **5.5.2 Shariah Scholars' roles, accountability and competence**

This study provided insight into the role of SSB members and, internal and external *Shariah* auditors who are responsible for ensuring all business dealings - products, services and transactions- are in line with the principles of *Shariah*. It is observed that Islamic companies in the three selected countries trust *Shariah* scholars and expect high degree of responsibilities and professionalism in accomplishing duties required. Although their accountability is to the only and one God, there could be a conflict of interest among *Shariah* scholars leading to agency behaviour. Therefore, there is need for independence for *Shariah* scholars and one possible way of addressing this, would be for the Government regulatory

body such as Market Authority or Monetary Authority to appoint *Shariah* scholars to work on the SSB for different companies and pay them the remuneration, while charging the companies for the service. Such arrangement is likely to mitigate principal- agent problem, conflict of interest and enables provision of quality and competent service. In addition, it is reported that there are some companies with a single scholar on the SSB, so there is a need to increase the number of SSB members in line with AAOIFI guidelines in order to ensure a *Shuratic* process, as provided by Islam, to deal with novel situations rather than rely on idiosyncratic decisions of an individual.

Overall, there is a shortage of *Shariah* scholars, which has led in past to some inadequacies in ensuring *Shariah* compliance, therefore there is a need for many qualified and trained *Shariah* scholars who specialise in “*Fiqh-al-Muamalat*” or knowledge of *Shariah* and finance to be able to serve in the commercial sector. While there are Islamic universities running Master’s and Doctoral programmes in *Shariah*, these would cover different *Shariah* laws affecting all aspects of life and many of the scholars trained on these programmes work in the legal profession or in advisory capacity in Government appointments.

Also, as a very few *Shariah* scholars have knowledge of both the Islamic and the conventional business practices, it is important for the Islamic companies or Government authorities to arrange for systematic training in contemporary business practices under experienced mentors to encourage better informed decisions and even suggestions for alternative products or services.

### **5.5.3 Implication and Recommendation for Management**

There are many CG related issues such as nepotism, small size BOD, lack of accountability, lack of independence due to family ties and lack of business competence. To improve the CG, it is necessary to have a clear and well-defined CG code of practice to be followed by all companies. Also, there should be management and contemporary business training for those joining the BOD on the basis of being family members or through inheritance. It must be noted that this may not apply wholly to UAE, where professional appointments are made on

BOD and the Government is proactive in ensuring better CG through supporting mechanism like 'Hawkamah' institution. In fact, UAE is also at forefront of applying *Shariah* CG in the Gulf region.

Moreover, there can be conflict of interest as the SSB members, the internal and external *Shariah* auditors are appointed by BOD. Transparency and disclosure for such appointments would be crucial to make sure the various stakeholders' interests are served.

In case of *Zakat*, any M&A will create a dual-taxation situation. This can happen even within two Islamic countries such as SA and Kuwait, both requiring payment of *Zakat*, thus duplicating the payment. While the low rate of *Zakat* at 2.5% may not create much problem, it could become significant when companies are not doing too well due to competitive pressure. The issue of dual-taxation, therefore, needs to be tackled as a matter of principle.

#### **5.5.4 Implication and Recommendation for Investors**

The research findings showed some challenges facing Islamic companies in M&A. The study also found that the owners of Gulf businesses have poor investment culture and lack relevant knowledge to evaluate the opportunities and risks to expand their businesses. Since the financial resources are pooled up from their friends and relations based on trust and loyalty, they do not know how or have experience to attract investments for large-scale growth, either organic or through M&A. Therefore, potential investors are advised to acquire skills and competence through training, business support, consultancy and participation in trade fairs. Investors are also needed to be cognizant of attracting foreign businesses with good business ethics and social responsibility.

*Shariah* principles ensure greater social justice and protection of the weak from exploitation by, for example, prohibition of interest, obligation to use *Zakat* for social welfare, prohibition of investments in alcohol, gambling etc. businesses which are considered social ills. The Islamic companies' products and services would, therefore, not only be of interests to the Muslim population throughout the world but also appeal to many ethical investors. However,

leaving *Shariah* compliance to individual idiosyncratic *Fatawa* is confusing and gives rise to uncertainty in the minds of non-Islamic investors. Therefore, there is a need for standardisation of Islamic products to avoid any confusion, as controversial interpretation of *Shariah* principles and contradicting *Fatawa* by different scholars on products such as *Tawarruq* will discourage non-Islamic investors.

Also, the lack of clarity and consensus amongst the scholars can lead to malpractice. When there has to be some margin of acceptance for prohibited practices, for example, when dealing with conventional business partners or in conventional markets some amount of interest related transactions may be unavoidable if the Islamic companies have to interact with global business. Ahmad (2009) pointed out that an Islamic company may be allowed to charge or pay interest at simple rates between 4% and 8%. However, as some scholars point out, such liberal interpretations can gradually lead more exceptions and further relaxations to ultimately allow the interest based systems to get well entrenched rather than being eliminated. It is therefore important to develop a widely-accepted consensus by scholars through a process of *Shura* about acceptable practices, develop an appropriate Islamic CG code and adopt it within the commercial law of the various countries.

## **5.6 Limitations and Suggestions for Future Research**

### **5.6.1 Limitations of the Study**

The research has answered all the research questions; however, there are some limitations, which are presented below:

First, in the Gulf countries, it is difficult for a woman researcher to get an agreement for interview. Particularly in the case of *Shariah* scholars, some scholars consider it a bad practice to interact with an unrelated female. A further complexity in Saudi Arabia is that, even when an agreement for an interview is obtained, the woman researcher needs to be chaperoned by the husband or a guardian which makes it difficult to arrange such meeting

depending on availability of all the three parties. In some cases, the concerned parties only agreed to skype or phone interviews and refused to meet in person.

Second, the researcher initially selected Qatar, Saudi Arabia and the UAE due to their high profile in investing abroad. However, due to the political tension between Saudi Arabia and Qatar at that time, it was difficult to find willing participants though efforts were made over a period of three months. In the circumstances, the choice of Qatar had been replaced with Kuwait as it is comparable to Qatar in banking and insurance sector.

Third, the theoretical framework was limited to three theories that have mostly been applied in conventional context of CG by researchers in previous studies. In order to provide a better explanation of some of the restrictive or conservative decisions by *Shariah* scholars, which might prima-facie be seen as based on subjective bias, alternative theories such as Legitimacy theory might have been useful. However, this would seek an explanation for conservative and literal approach, when Islam allows alternative decisions based on the current context. This would involve a separate discussion on the tension between a decision-making process based on knowledge and that based on wisdom.

Fourth, the research concentrated on the Islamic companies in the banking and insurance sectors in the Gulf countries by focusing on the key stakeholders such as the members of SSB and BOD, managers and lawyers; which was adequate for the purpose. Perhaps, a richer picture could have emerged if there was a dialogue with the family-member owners who are not active in managing the business, minority shareholders, managers of non-Islamic companies and the *Shariah* auditors. However, it is very difficult to get access to the non-managing owners, individual minority shareholders or the key managers of non-Islamic companies as they would be based abroad. Since internal auditors are only concerned with the implementation the SSB decisions, they may throw some light on the practical implementation problems but cannot explain the strategic decision-making process. The external *Shariah* auditor is a relatively new practice only adopted in UAE and is in a nascent stage. However, in future, this could be a good source of information on *Shariah* compliance.

Fifth, the sample size was sufficient to draw the main conclusions and the sample was representative as the overall findings confirmed the initial findings from the pilot study. A greater number of participants at various levels in the organisation could have contributed a possibly greater range of opinions. However, this would have involved much greater cost and time-delays as it was very difficult to obtain access to these individuals and get their agreement. Also, some of the *Shariah* scholars might have been less forthcoming in the interviews due to sensitivity of the topic and they might not want to be critical of either the fellow scholars or the management.

Sixth, the research was undertaken in three out of the six Gulf countries. While this approach may have given a good range of divergent practice based on differing levels of orthodoxy and is likely to cover the practices in the remaining three countries, there might be some variations based on local culture. Similarly, there might be diversity of practices if the findings of this study are to be projected to Islamic companies in other parts of the world, for example, Malaysia, Indonesia, Bangladesh or Pakistan.

Seventh, Islamic CG is still in a development stage and mainly focussed on the Islamic financial instruments. While *Shariah* compliance is achieved mainly by avoiding the prohibited practices, some tolerance and compromises are being proposed, accepted, tested and refined with experience. Some of the findings will be based on the current state of *Shariah* CG and the relatively low volume of M&A between the Islamic and non-Islamic companies. This might change over time.

Finally, due to the religion connection, any critical observation on an ethical issue may be misconstrued as criticism of a religious belief or practice by some ultra-conservative followers, which could pose potential danger especially if the findings of the study are presented in an Islamic society. The researcher would like to emphasise that the researcher believes the *Shariah* principles to be just and socially beneficial. Following these principles can ensure greater social welfare in the capitalist business practices. Any critical discussion is directed at shortcomings of the human behaviour and individual failures on the part of those involved in the *Shariah* compliance.

### **5.6.2 Suggestions for Future Research**

First, cross-border M&A have been used by large organisations to strategically expand their business across the globe. Many researchers have studied cross-border M&A within the developed countries, where though there are cultural variations; there is a commonality in terms of acceptance of the Western business model (for example, Rossi & Volpin, 2004; Hennart & Reddy, 1997). There is hardly any literature on companies in the developing countries where the culture integrates strong religious beliefs which do not only address spiritual matters but the whole way of life. While this study has looked three Gulf countries, future research can look at *Shariah* compliance in other parts of the world.

Second, this study is based on the Stakeholder theory, Stewardship theory and Agency theory. However, there can be other theoretical perspectives; for example, Legitimacy theory which can help us better understand the unique features and practices of Islamic companies and contribution these can make to the wider management, organisational and even corporate social responsibility literature.

Third, although many researchers have emphasised the complexity involved in any cross border M&A, there is little research on the cross-border M&A involving Islamic companies. This study has identified the main barriers of such M&A involving Islamic banks and insurance companies in three Gulf countries. There is considerable scope of identifying the barriers in other industries, such as Tourism, Travel as the demand for *Shariah* compliant business grows and there is increasing diversification away from Oil based economy.

Four, there is hardly any research on the rate and causes of failure of cross-border M&A between Islamic and non-Islamic companies. Learning from such failures will assist the future M&A in avoiding failures as well as saving a lot of costs and time-delays. Such literature will also inform the emerging institutions like AAOIFI, IFSB etc. concerned with *Shariah* governance, in formulating commonly accepted Islamic standards.

Six, many researchers have pointed out the problem of dual-taxation arising in cross-border

M&A and agreements between countries to avoid this. Similarly, there is an issue of dual *Zakat* in case of M&A between two Islamic companies in countries where *Zakat* is compulsory. Generally, companies may not consider this as a big issue as *Zakat* is only payable at 2.5%, however, in future when the Islamic companies engage in competitive industries, even this low rate of *Zakat* may unfavourably impact the profitability. There is scope for research on what the right approach to determine the *Zakat* payable is and how to avoid the situation of dual-*Zakat* payments.

## **5.7 A Final Note on the Initial Research Objectives**

In the Introduction of this thesis, the researcher stated the purpose of the thesis was to examine the influence of *Shariah* CG on the cross- border M&A between Islamic and non-Islamic financial companies and set seven research objectives. The first research objective sought to identify how the Islamic corporate governance is constituted and its difference from the conventional corporate governance model, while the second was to examine to what extent the Islamic CG is adopted by the companies. Both the research objectives have been sufficiently addressed. In chapter four the researcher, using thematic analysis, found similarity in main CG principles of the two CG models but companies in these three countries could not adopt any conventional code of practice without evaluating it on the Islamic *Shariah* principles and culture. However, the finding of the study also showed that Western companies are willing to work with Islamic companies in the Gulf countries with great care and that they have an adequate understanding of the need to comply with the *Shariah* principles (4.6.2). In terms of second research objective the findings of this study showed variations among the three countries regarding the extent to which Islamic CG model is adopted and the level of awareness of employees of the CG principles.

The third objective of the thesis sought to examine how the current Islamic CG mechanism practised in the three countries enable or constrain the process of cross-border M&A and which cultural factors influence the Islamic CG mechanisms. The analysis of interviews showed that whilst the financial reporting and disclosure could be quite similar between conventional and Islamic principles, there were differences in the degree of implementation



across the sectors and the countries (see section, 4.3.1), and the non-existence of clear code of conduct. The study further showed that composition and the size of board, the ownership structure, the level of disclosure and transparency and gender segregation combined enable and/or constrain the effectiveness of the Islamic corporate mechanisms (sections 4.3.2 & 4.3.3 & 4.5.1 & 5.2 key finding 2). The fourth research objective sought to explore to what extent *Shariah* principles were used in business practices of Islamic financial companies and to identify active players in interpretation and enforcement of these principles. The study found that though such principles were adhered to and applied, there were inconsistencies and lack of uniform application across the cases or countries. Furthermore, the findings showed *Shariah* scholars and *Shariah* Supervisory Board to be influential actors in enforcing the incorporation of Islamic principles in business practices such as screening provision of products and service in these three countries (see sections, 4.4.1 & 4.4.2 & 4.6.1) and strict application could be restrictive in the process of cross- border M&A (4.3.2 & 4.6.1)

The fifth objective set to identify the main barriers for effective implementation of the *Shariah*- based Islamic CG principles in business and in the context of cross-border M&A. This research objective was addressed in various sections of the data analysis. The main findings included difficulties of knowing deficiency of the advice provided regarding *Shariah* compliance, underdevelopment of relevant infrastructure, inadequate or limited business knowledge by management, BOD, SSB members of the Western business context, under defined or emergent legal provisions in support of *Shariah* principles, low level awareness of the conventional CG, its code of conduct and possible cause of variations in *Shariah* compliance which highlighted the difference between the presumed stewardship behaviour and the reality of agency behaviour.

Research objective six sought to examine the nature and influence of the Islamic legal corporate structure on the decision- making process in Islamic companies. The finding of this study showed: a) in all the three countries, there is no clear well-defined legislation on how Islamic companies engage in M&A locally or at overseas locations; b) the three countries adopted different stances from passive (market-driven in Saudi Arabia), minimalist intervention of law ( Kuwait), to ensuring compliance with external Sharia audits in UAE ( see, 4.4.3).

Final research objective was to identify the M&A financing instruments used in the context of cross-border M&A. It was found that *Sukuk* was the most widely used but costly financial

instrument in cross-border M&A activities as it fully complies with *Shariah* principles whereas *Tawarruq* is considered questionable in terms of *Shariah*.

In summary, all the research objectives were addressed with rigour and helped to achieve the research purpose. All the research objectives were supported with sufficient empirical evidence, corroborated with previous extant work and thus provided relevant contributions for theory, policy and practice in the study areas.

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## APPENDICES

### Appendix 1: Inheritance according to Islamic *Shariah* Law

#### **Mawarith-** An Islamic Inheritance Calculation Program

***Qur'an 4:11*** Allah commands you as regards your children (inheritance),

To the **MALE**, a portion equal to that of **TWO FEMALES**;

If (there are) only **DAUGHTERS**, two or more, their share is **TWO-THIRDS** of the inheritance;

If only one, her share is **HALF**.

For **PARENTS**, a **SIXTH** share of inheritance to **EACH** if the deceased left **CHILDREN**;

If **NO CHILDREN**, and the **PARENTS** are the (**ONLY**) heirs, the **MOTHER** has a **THIRD**;

If the deceased left **BROTHERS** or (**SISTERS**), the **MOTHER** has a **SIXTH**.

(The distribution in all cases is) after the payment of legacies he may have bequeathed or debts. You know not which of them, whether your parents or your children are nearest to you in benefit. (these fixed shares) are ordained by Allah. And Allah is Ever All-Knower, AllWise.

***Qur'an 4:12*** In that which your **WIVES** leave, your share is a **HALF** if they have **NO CHILD**;

But if they leave a **CHILD** you get a **FOURTH** of that which they leave after payment of legacies that they may have bequeathed or debts.

In that which **YOU** leave, their (**YOUR WIVES**) share is a **FOURTH** if you have **NO CHILD**;

But if you leave a **CHILD** they get an **EIGHTH** of that which you leave after payment of legacies that you may have bequeathed or debts.

If the **MAN** or **WOMAN** whose inheritance is in question has left **NEITHER ASCENDANTS NOR DESCENDANTS** (Al-Khalala), but has left a **BROTHER** or a **SISTER**, **EACH ONE** of the two gets a **SIXTH**; but if **MORE THAN TWO**, they share in a **THIRD**; after payment of legacies he (or she) may have bequeathed or debts, so that no loss is caused (to anyone).

**THIS IS A COMMANDMENT FROM ALLAH**; And Allah is Ever All-Knowing, Most-Forebearing.

***Qur'an 4:176*** They ask you for a legal verdict, Say, "Allah directs (thus) about Al-Khalala (those who leave neither ascendants nor descendants as heirs).

If it is a **MAN** that dies, leaving **A SISTER** but **NO CHILD**, **SHE** shall have **HALF** the inheritance.

If (such a deceased was) a woman, who left **NO CHILD**, her **BROTHER** takes her **INHERITANCE**.

If there are **TWO SISTERS**, they shall have **TWO-THIRDS** of the inheritance;

If there are **BROTHERS** and **SISTERS**, the male will have **TWICE** the share of the female.

(Thus) does Allah make clear to you (His Law) lest you go astray. And Allah is the AllKnower of everything.

#### **LEVEL I - PRIMARY (Immediate) HEIRS**

The primary (or immediate) heirs classified as Level I are:-

1. The **SPOUSE** (Husband or a maximum of four Wives)
2. The **CHILDREN** (Sons and Daughters)
3. The **PARENTS** (Father & Mother)
4. The **GRANDCHILDREN** (Sons's SON or Son's DAUGHTER only)

(applicable only when the SON is already deceased only and has offspring)

#### **LEVEL II - SECONDARY HEIRS**

The secondary heirs classified as Level II are:-



1. The **GRANDPARENTS** (Paternal and Maternal)
2. The **BROTHERS** and/or **SISTERS** (In the absence of Father and Son ONLY)
3. The **UNCLES** and/or **AUNTS** (In the absence of Grandparents ONLY)
4. The **NEPHEWS** and/or **NIECES** (In the absence of Brothers and Sisters ONLY)

Note: It is not practical to go beyond Grandparents as the chances of Greatgrandparents surviving before you is not very high. However, the logic is that in the absence of a particular heir, the next level becomes eligible for inheritance. Eg; IF the Grandparents are dead THEN the Great Grandparents are entitled (if living only) and so on. It is better, for practicality and convenience to limit the inheritance level up to The GrandParents and the Grandchildren. If we attempt to go beyond these levels there will be no limit to the program logic validation.

Under Islamic Law, the primary beneficiaries of a deceased person are his/her IMMEDIATE (Level I) Heirs. ie; Spouse(s), Children, Parents and Grandchildren (if children are deceased only). The Grandchildren that are entitled are only the Son's Son or the Son's Daughter. Daughters children are not entitled even if the Daughter is deceased.

In the absence of some or all of these heirs the secondary beneficiaries (Level II) become Heirs under various conditions. In the absence of a particular Heir (eg; Uncle) if and when he/she is entitled the children of that Heir become eligible.

### **LEVEL I - Inheritance Logic:**

#### **1. SHARE OF HUSBAND**

IF NO ENTITLED DESCENDANTS EXIST (ie; Children/Grandchildren)

THEN

**HUSBAND = 1/2**

IF ENTITLED DESCENDANTS EXIST (ie; Children/Grandchildren)

THEN

**HUSBAND = 1/4**

Note: ENTITLED DESCENDANTS = Sons, Daughters, Son's Son, Son's Daughter.  
Daughter's children are NOT entitled.

## **2. SHARE OF WIFE**

IF NO ENTITLED DESCENDANTS EXIST (ie; Children/Grandchildren)

THEN

**WIFE = 1/4**

IF ENTITLED DESCENDANTS EXIST (ie; Children/Grandchildren)

THEN

**WIFE = 1/8**

Note: ENTITLED DESCENDANTS = Sons, Daughters, Son's Son, Son's Daughter.

Daughter's children are NOT entitled.

## **3. SHARE OF DAUGHTER'(s)**

IF ONLY ONE DAUGHTER (and NO Sons)

THEN

**DAUGHTER = 1/2**

IF TWO OR MORE DAUGHTERS ONLY (and NO Sons)

THEN

**DAUGHTERS = 2/3**

(to be shared equally between all of them)

IF both SON's & DAUGHTERS EXIST,

THEN

**SON:DAUGHTER = 2:1**

## **4. SHARE OF FATHER**

IF ENTITLED DESCENDANTS EXIST

(Sons, Daughters, Son's Sons, Son's Daughters)

THEN

**FATHER = 1/6**

IF NO MALE DESCENDANTS EXIST (Sons, Son's Sons)

THEN

**FATHER = 1/6 plus Residue**

(residue = remainder after all legal shares are distributed)

IF NO ENTITLED DESCENDANTS EXIST

THEN

**FATHER = Residue 5. SHARE OF MOTHER**

IF ENTITLED DESCENDANTS or BROTHERS/SISTERS EXIST

THEN

**MOTHER = 1/6**

IF NO ENTITLED DESCENDANTS EXIST

THEN

IF NO BROTHERS/SISTERS, NO FATHER, NO SPOUSE EXIST

THEN

**MOTHER = 1/3**

IF BROTHERS/SISTERS, FATHER, or SPOUSE EXIST

THEN

**MOTHER = 1/3 of Residue 6. UTERINE BROTHER/SISTER ( from same Mother, different father)**

IF ONE UTERINE BROTHER/SISTER EXIST

THEN

IF NO ENTITLED DESCENDANTS and NO MALE ASCENDANTS

(Father/Father's Father etc)

THEN

**UTERINE BROTHER = 1/6 or UTERINE SISTER = 1/6**

IF TWO OR MORE UTERINE BROTHERS/SISTERS EXIST

THEN

IF NO ENTITLED DESCENDANTS .AND.NO MALE ASCENDANTS

(Father/Father's Father etc.)

THEN

**ALL UTERINE BROTHERS & SISTERS = 1/3**

Note: If there are UTERINE Brothers/Sisters IN ADDITION to FULL Brothers/Sisters (same father/mother), then they share in the residue.

## **7. SHARE OF SON'S DAUGHTER**

IF ONE SON'S DAUGHTER EXIST

THEN

IF NO DAUGHTERS EXIST

THEN

IF NO SON'S SON EXIST

THEN

**SON'S DAUGHTER = 1/2**

IF SON'S SON EXIST

THEN

**SON'S DAUGHTER = HALF SHARE OF SON'S SON**

(ie Son's SON share: Son's DAUGHTER share = 2:1)

IF TWO OR MORE SON'S DAUGHTERS EXIST

THEN

IF NO DAUGHTERS EXIST

THEN

IF NO SON'S SONS EXIST

THEN

**SON'S DAUGHTERS = 2/3 (equally between them)**

IF SON'S SON EXISTS

THEN

**SON'S DAUGHTER = HALF SHARE OF SON'S SON**

(ie Son's SON share: Son's DAUGHTER share = 2:1)

## **8. SHARE OF FULL BROTHER/SISTER**

(Full Brother/Sisters are brothers/sisters from the same FATHER & MOTHER)

**Brothers & Sisters inherit ONLY when there are NO Descendants (Son/Sons, Son's son etc.) and NO Ascendants (Father/Grandfather etc.)**

The arabic word "**AL-KHALALA**" is used in the *Qur'an*, Chapter 4 - Al-Nisa, Verses 12 & 176, which is translated by almost all the translators of the *Qur'an* to mean "Ascendants & Descendants" thus giving rise to the interpretation that they include "Parents and Children".

However, many scholars have preferred to classify the word as meaning "Father or Son" thus excluding the female components of both Ascendants and Descendants (mother & daughters).

IF NO FULL BROTHER and NO FEMALE ENTITLED DESCENDANT EXIST

(daughter, Son's daughter etc.)

THEN

IF deceased was MALE,

THEN

**FULL SISTER =  $\frac{1}{2}$**  (if only ONE)

IF NO FULL SISTER and NO FEMALE ENTITLED DESCENDANT EXIST

THEN

IF deceased was FEMALE,

THEN

**FULL BROTHER = 1** (if only ONE)

IF TWO OR MORE BROTHERS & SISTERS

THEN

**FULL SISTERS =  $\frac{2}{3}$**  (shared equally between them)

**FULL BROTHER's & SISTER's** (combination) = 2:1

IF NO FULL BROTHER EXIST but FEMALE ENTITLED DESCENDANT EXIST

(daughter, Son's daughter etc.)

THEN

**FULL SISTER =  $\frac{1}{6}$**  (if only one)

IF NO FULL SISTER EXIST but FEMALE ENTITLED DESCENDANT EXIST

THEN

**FULL BROTHER =  $\frac{1}{6}$**  (if only one)

IF FEMALE ENTITLED DESCENDANT EXIST

THEN

**FULL SISTERS & BROTHERS =  $\frac{1}{3}$**  (share equally) **9. CONSANGUINE SISTER**  
(Sister from same Father but different Mother)

**Consanguine Sisters inherit ONLY when there are NO SON's or Son's SON(s) AND NO FATHER AND NO FULL BROTHER.**

IF ONLY ONE FULL SISTER AND NO CONSANGUINE BROTHER

THEN

**CONSANGUINE SISTER** (if only one) =  $\frac{1}{2}$  **CONSANGUINE SISTER(s)** (if two or more) =  $\frac{2}{3}$

IF ONE FULL SISTER AND CONSANGUINE BROTHER(s)

THEN

**(CONSANGUINE) BROTHER:SISTER = 2:1 10. TRUE GRANDMOTHER**

**True Grandmother is defined as the one whose line of connection with the deceased is NOT interrupted by a MALE between two FEMALES. They are entitled ONLY if the FATHER or MOTHER do not exist.**

Eg; Mother's MOTHER, Father's MOTHER

Father's Father's MOTHER, Mother's Mother's MOTHER

**TRUE GRANDMOTHER =  $\frac{1}{6}$  11. TRUE GRANDFATHER**

**True Grandfather is the one whose line of connection with the deceased is NOT interrupted by a FEMALE between two MALES. They are entitled ONLY if the Father or Mother do not exist. Eg; Father's FATHER**

Father's Father's FATHER

Mother's FATHER

Mother's Father's FATHER

**TRUE GRANDFATHER =  $\frac{1}{6}$  IF MALE DESCENDANTS EXIST (Son, etc)**

**TRUE GRANDFATHER =  $\frac{1}{6}$  + Residue IF FEMALE descendants exist**

**TRUE GRANDFATHER = Residue IF NO Male/Female descendants exist**

**12. UNCLES & AUNTS (Father's/Mother's Brothers & Sisters)**

Uncles and Aunts are ONLY entitled in the absence of GRANDPARENTS. This means that they will receive shares ONLY if there are NO Parents AND Grandparents because Grandparents do not inherit when the Parents are living. They will also NOT inherit if the

children (or children's children) of the deceased are living. Proportions here are also in the ratio of 2:1 for Male:Female.

### **13. NEPHEWS & NIECES (Children of Brothers/Sisters)**

Nephews and Nieces are ONLY entitled in the absence of Brothers and Sisters. This means that they take the shares of the Brothers/Sisters of the deceased in their absence. Hence a Nepew/Niece will receive what his/her parent (Brother/Siuster of the deceased) would have received if he/she was alive. They will also NOT inherit if the children (or children's children) of the deceased are living. Proportions here are also 2:1 for Male:Female.

## **Appendix 2: Request for Interview**

My name is Wardah Bindabel. I am a PhD student in the UK; I am presently working on a study to investigated impact of *Shariah* on cross-border M&A in gulf countries (Saudi Arabia, Kuwait and UAE), between Islamic and non-Islamic companies. I have been able to identify some cooperate governance implications of Cross-border M&A with companies in Islamic countries which are crucial for my research due to *Shariah*-compliance issues.

Despite the economic growth in Gulf countries, enquiry into corporate governance practices has focused mainly on the conventional corporation with very limited attention given to Islamic corporations. Corporate governance is a vital element of any corporation and presents even greater challenges to Islamic corporations, taking into account the additional risks that characterize Islamic corporations.

I believe doing interview (with you) will go a long way to provide me with important information/data that would help this study. I would like to assure you that no transfer of data or information will take place without prior consultation, all information is required solely for this research and any data collected will comply with data protection law.

Please accept the assurance my highest regards. Please do contact me if you need more information about the research and interview.



Thank you very much for your time and consideration.

Yours faithfully,

### **Appendix 3: Interview Questions for Lawyers**

1. What sector of the market are you specialized in?
2. How long have you been practicing in this area?
3. Have you been ever involved in cross-border M&A deals?
4. What were the reasons behind M&A transactions?
5. What are the legal issues would be able to consider beforehand to ensure that your business is in perfect alignment for M&A deals?
6. From your experience what is likely to go wrong when formulating the deals with non-Islamic companies?
7. What is the role of internal and external audit during M&A?
8. During due diligence, what is the potential risk, or control or regulatory issues that would cause failure of M&A?
9. Are there any obstacles/ restrictions of growth particularly with the cross-border deals in respect to *Shariah* law?
10. What are the risks related to the variations in the *Shariah* based systems across Gulf countries?
11. What are the main differences in the CG practices between the Gulf and Western countries?
12. In the event of cross-border M&A, what are the mechanisms of the company that allow all stakeholders to express the opinion?
13. How can you describe the Muslims' investors understanding of M&A?
14. How would you describe the role of tax regime in the Gulf region in M&A?
15. What is your perception on the impact of Islamic principles on M&A? for example:
  - Principle of *Zakat*
  - Impact of prohibited deals such as *Riba*
  - Limited Islamic financial products
16. Are there be written Islamic corporate governance that might make or cut short M&A?
17. What would be your assessment of the level of corporate disclosure in the region?

18. Since each company has the right to choose the SSB members, does this rise the issue of conflict of interest?
19. ARE there any cultural issues (such as women in workplace, business culture and decision making process) that might affect M&A?

#### **Appendix 4: Interview Questions for *Shariah* Supervisory Board**

1. What is your job description? How long you have been practicing in this area?
2. What is the ultimate goal of Shariah Board in an Islamic company?
3. What is the required qualification or expereice for *Shariah* board member's position?
4. Concidering the rapid growth of Islamic finance, is there a suffecint number of scholars who combine the qualifications and experience needed?
5. Who assign or appoint SSB members of the company's Board?
6. What are the criteria you use for such appointment SSB and are they externally or internally appointed?
7. Is conflict of intrest applicable to external *Shariah* scholars when reviewing Shariah documents and issuing a fatwa?
8. Are young *Shariah* scholars given the chance to serve on Sharia boards? If no why?
9. How jurisprudential decision members should be issued?
10. Are multiple positions in more than one company negatively affects Shariah compliance?
11. How would you describe the role of *Shariah* Board members and how would *Shariah* scholars operate effectively in an Islamic company?
12. What are the challeges that *Shariah* Board members face in an Islamic company?
13. What are the benefits of Sharia compliance?
14. How do you describe the relationship between Board members and *Shariah* Board members and how their roles differ from in the company?

15. Do you think the formation of other committees of *Shariah* compliance such as external *Shariah* Auditing will enhance the process of accountability?
- If no, why?
  - If yes, how?
16. Do you think the establishment of a committee in charge of *Shariah* compliance which would ensure compliance across the Gulf countries has an impact on the performance of Islamic companies?
17. In your opinion, what would you consider to be the main risk of the financial reward given to SSB members? do you think this will impact the ethics of their role?
18. To what extent would you argue that differences in the interpretation of *Shariah* across different companies and across Gulf countries with respect to M&A?
19. What is the role of *Shariah* board members in the formation of M&A at an international level?
20. Which authority is responsible to agree the *Fatawa*?
21. What is the impact of irresponsible fatwas on the expansion of Islamic companies?
22. How can we avoid possible differences in the application of *Shariah* law with respect to M&A whether in the same country or across Gulf countries?
23. In your perspective, how important is the inventing of products to fund international M&A with non-Islamic companies? What products do Islamic companies use to fund such deals?
24. Does the *Shariah* Board composition include women?
- If yes, what is their rule
  - If no, why?
25. What are the religious and cultural issues that could prevent/limit M&A?
26. Are there any alternatives for Islamic firms to compete with conventional companies without affecting *Shariah* law?

## Appendix 5: Interview Questions for Managers

1. What is your job description? And how long you have been practicing in this area?
2. How old is your establishment?
3. What is the ultimate goal of *Shariah* governance? Are there any written rules and regulations?
4. What CG model does your company adopt? Are there any differences between *Shariah* CG and conventional CG?
5. What factors do you consider when adopting any conventional CG code?
6. How would you describe the awareness of your employees about CG? What efforts have you undertaken to improve quality awareness within your organisation?
7. What is the ownership structure of your company?
8. What is the Board size of your company and is there any negative impact of family members being presented in the Board?
9. What is the impact of external investor on the company?
10. Does your company comply fully with the *Shariah* law?
  - A\_ If the answer is No, does your company partly comply with the *Shariah*? In which area does your company comply with *Shariah* law and why?
11. How would you ensure *Shariah* compliance in your company?
12. How would you evaluate the level of disclosure of *Zakat* of your company?
13. How does *Shariah* law affect the firm's management?
14. What are the challenges of complying with the *Shariah* law?
15. Who assign or appoint SSB members of the company?
16. What are the criteria you use for such appointment, are they externally or internally appointed?
17. Does the Government pressure affect the belief altruism (devotion or selfless concern) of your company?
18. Does *Shariah* law encourage or limit practicing in M&A deals?
19. What would you consider as the key drivers that drive your company to engage in cross-border M&A?

20. What are the complex procedures of *Shariah* compliance in terms of M&A?
21. How does your company assess its performance under the *Shariah* law, what are your anticipated benefits from investing in Islamic companies?
22. How would you describe the role of SSB of your company and what are the challenges you face with SSB?
23. What impact do SSB members have in your company's investment decisions?
24. In your opinion, what would you consider to be the main risk of the financial reward given to SSB members?
25. How different fatawa given by different *Shariah* scholars impact on Islamic companies' performance and expansion?
26. How would you describe SSB members' understanding and appreciation of the key operation, management and strategic issues of your company?
27. In the event of cross-border M&A, what are the mechanisms of the company that allow all stakeholders express their opinion?
28. What efforts have been made to ensure adequate mix of skills and experience among BOD members and SSB of your company to overcome the challenges of Islamic companies?
  - By way of training and retraining
  - Increasing BOD knowledge about Islamic law in relation to your company operations and increasing SSB knowledge about business operations.
29. What are the challenges you might face with non-Islamic companies when following strict *Shariah* compliance?
30. How would you describe non-Islamic companies' understanding of the need of *Shariah* compliance?
31. What is the position of Islamic inheritance law? Does it affect M&A?
32. Which Islamic instrument do you use to formalise businesses that comply with *Shariah* across international boundaries?
33. Are there any religious and cultural factors affect M&A?

## **Appendix 6: Conference Paper Presented**

**Conference:** Sydney International Business Research Conference (SIBRC) 2016, Sydney, Australia \_ 19-21 March 2016.

**Title of the Paper:** The challenges faced by integrating Islamic Corporate Governance in companies of Gulf countries with Non-Islamic companies across border through Merger and Acquisition.